

1

Context

On the first of July 2013, Croatia became the 28th member country of the European Union, a decade after it started the process of ascension and less than 20 years after the end of its war of independence from Yugoslavia. Croatia is the first country to join the EU since 2007, when Bulgaria and Romania came on board, and only the second of the seven ex-Yugoslav states after Slovenia was part of the big bang eastward enlargement in 2004.

In Brussels, Croatian membership equates to one extra EU commissioner - in charge of Consumer Affairs - and 12 members of the European Parliament. But the country's membership comes at a difficult time for both parties. The EU is mired in high unemployment and low growth, and in an almost constant state of bickering as it tries to overcome its Eurozone crisis and integrate further. Croatia, with an unemployment rate of over 20%, has an economy that has for the past four years either been in recession or stagnant.

Croatia was heavily damaged by war and post-socialist economic adjustments through the mid-1990's. Microfinance was one of the tools employed to assist those who turned to self-employment in order to support themselves and their families. The first investment of the international microfinance network in Croatia was in 1996, when Opportunity International facilitated the founding of NOA Savings and Loan Cooperative (SLC), the first Croatian MFI, to begin lending operations in the war-torn region of Eastern Slavonia. NOA registered as an SLC, utilizing the only available institutional form for microfinance. Two more microfinance institutions, MikroPlus and DEMOS SLC, were founded in 1999 and 2000, respectively.

With USAID support, by 2007, these organizations had grown to roughly 6,000 clients with a portfolio of over EUR 6.5 million and were able to fulfill their mission of supporting un-bankable clients with micro-loans mainly located in the rural war-affected areas of Croatia. In 2008, USAID ceased operations in the country but had left the MFIs on a path of sustainable growth.



2

Objectives of the Mapping Exercise in Croatia

However, a number of challenges were faced by these three microfinance organizations due to the restrictive regulatory environment, in that SLCs could not borrow externally, client savings were not included in the Croatian depository insurance scheme, and weaknesses in the law reduced the effectiveness of SLCs' governance structures. The environment was further degraded by changes in the regulatory environment that took place in 2008, as described below.

In this context, the objective of the mapping exercise in Croatia is to identify the key stakeholders of the microfinance sector, to map their interest and capacity in lobbying for the creation of an enabling legal framework, contribute to the development of an efficient and effective microfinance sector capable of serving the un-bankable entrepreneurs, and to benefit the socio-economic development of the country within the European Union context.

3

Existing legal framework for MF provision assessment

A Primary and secondary regulation for the Croatian financial sector, gaps identified, compliance with EU regulations (ECGC), proposals for new regulations, etc.

In December 2008, the Croatian Parliament, at the proposal of the Ministry of Finance with the support of the Croatian Central Bank, passed a new law abolishing Savings and Loan Cooperatives and mandating their transformation into either Savings Banks or Credit Unions.

These transformation options were illusory, however, as the Croatian Central Bank rejected all SLC applications for transformation into Savings Banks, with a single exception. Consequently, all of the 50+ SLC applications for a Savings Bank license were rejected forcing the 121 SLC's into the unpleasant choice of liquidation or becoming a Credit Union.

The new legal framework that provided for the transformation of SLCs into Credit Unions was even more problematic than the earlier SLC law. The new law restricted Credit Union operations to only one "zupanija" (county), most of which have fewer than 40-50,000 inhabitants. This made the potential market extremely small, and also reduced the ability of the Credit Union to operate with sufficient scale to ensure sustainably.

There is also a continuing ban on the ability to borrow loan funds externally, and the Credit Unions each require at least 30 founders who all must also be from the same zupanija and must contribute at least EUR 70,000 in founding capital. As with the SLC framework, deposits are not guaranteed and all payments must be made through the banking system.

The law puts Credit Unions in a very unfavorable position relative to banks and also makes it extremely difficult for them to reach sufficient scale to operate sustainably. As a result, the 121 SLC's were quickly whittled down to just 36 Credit Unions, of which 10 are already in bankruptcy or liquidation. In terms of microfinance, the law abolishing SLC's drove two out of the three MFI's into liquidation with a loss of donor funding over EUR 3 million

B Current Situation

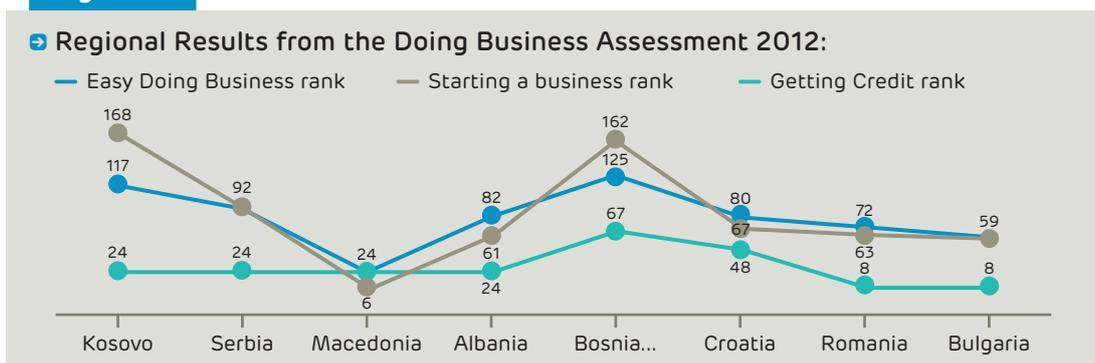
Despite various uncoordinated efforts of microfinance practitioners to influence policy development, the only institutions permitted by law to engage in lending in Croatia at this time are commercial banks and Credit Unions. Commercial banks at the time did not (and still do not) serve microfinance clients: they were seen as too risky due to their lack of business history, experience, collateral, and geographic location. Thus the SLC framework, despite its weaknesses, was the only possible one for microfinance.

Foundations, NGOs that are frequently found in other countries in the region (e.g. in France and Spain), Non-bank financial institutions or finance companies found mainly in central and eastern Europe (e.g. in Bulgaria, Romania or Poland) or government funded networks or associations (e.g. in Germany and Hungary) are not allowed by the current legal framework in Croatia to become venues for loan distribution, regardless of the proven social and economic impact of microfinance on the un-bankable clients and beneficiaries from vulnerable groups: unemployed, farmers, individual entrepreneurs, micro-enterprises, ethnic minorities, etc.

As a consequence, according to the "Doing Business Assessment Report 2012 of the World Bank"¹, access to finance for investment and income generation activities for SMEs and entrepreneurs is more difficult in Croatia, which ranked 48, than in all of its neighboring countries (e.g. Romania and Bulgaria, ranked 8) where the legal framework allows a larger extension of Non-Bank financial institution lending to provide a range of financial services: including credits, leasing, mortgage, guarantee and counter-guarantee, etc. as presented in the figure below.

¹ World Bank/ IFC – Doing Business report 2012 – Doing business in a more transparent world – comparing regulation for domestic firms in 183 countries; How economies rank – from 1 to 183 www.doingbusiness.org/Rankings

Figure 1



4

Mapping of Stakeholders and Sponsors of the Legal Framework Initiative

The main identified stakeholders of the microfinance sector in Croatia are the following:

- ➔ The **individual Credit Unions and the Unions of Credit Unions** (county and national apex structures, Association of Credit Unions)

Their interest is to lower the registration entry barrier (minimum initial capital and number of founders) and obtain permission to lend to clients located in a larger geographical area.

- ➔ The **existing microfinance institutions** financed and assisted by international donors represented by DEMOS

Their interest is to promote a new legal framework allowing registration or transformation into Non-Bank Financial Institutions (NBFI), similar to the MFIs- NBFI in Bulgaria, Romania and Poland, operating under the guidance and according to the quality standards of the European Code of Good Conduct for Microcredit Provision in the European Union.

- **Representatives of the beneficiaries/ potential beneficiaries:** Croatian Employers Association, Chamber of Commerce, Croatian Chamber of Trades and Crafts, Croatian Coop. Association, Croatian Employment Service, Workers Unions, Professional associations: accountants, architects, private medical practices, etc.

Their interest is to improve access to financial resources and business development support services (BDSS) and create an enabling environment for fair competition among the actors on the financial market in Croatia, leading to improved quality of financial services.

- **Representatives of the Croatian Government:** Ministry of Finance, Ministry of Economy, Ministry of Justice, agencies and departments dealing with financial sector and private sector especially SMEs, Ministry of Regional Development and EU Funds, Ministry of Entrepreneurship and Crafts.

Their interest is to contribute to the creation of an enabling environment for economic development and to improve the legal framework for doing business in Croatia, including access to financial and BDSS resources and services for assistance and co-financing beneficiaries of SMEs and entrepreneurship development grant programs financed by the structural funds within the following EC's financial program 2014-2020.

- **Representatives of the financial sector, Regulators/policy makers and actors: Central Bank, Croatian Bank for Reconstruction and Development, EBRD, World Bank, Banks, investors, insurance companies.**

Their interest is to maintain the solidity of the financial sector in general; therefore, the entry barriers, extension of the prudential rules and supervision by the Croatian Central Bank of the non-bank financial sector are among the sensitive issues commercial banks and regulators are lobbying for with the primary focus being on sectorial stability.

Improvement of Microfinance Legal and Regulatory Framework – Lobbying Strategy

In an effort to organize a response by the microfinance sector to the current hostile legal environment for microfinance activities, the EMN's Legal Environment and Regulation Working Group (LER-WG) met in Croatia in April 2013. The goal LER-WG meeting was to hear from all relevant stakeholders and to discuss a possible alternative legal framework for the provision of microfinance services in Croatia.

The meeting was attended by key stakeholders from the microfinance sector in Croatia:

- Representatives of individual Credit Unions in Croatia;
- Leaders of the two Federations of Credit Unions in Croatia;
- From the government side, a representative of the Croatian Central Bank.

The result of the meeting was the initiation of a lobbying effort to be organized around drafting a new microfinance law in Croatia aimed to develop the financial sector in accordance with EU regulations, in order to facilitate access to finance for underserved small business and create jobs.

An enabling legal environment for microfinance in Croatia is estimated to contribute to the creation of over 20,000 jobs within a few years, generate EUR 10 million in additional tax and PDV payments, and attract up to EUR 50 million of direct investment by social investors, EU funds, and microfinance actors.

At the conclusion of the meeting, it was clear that there was a great deal of interest for stakeholders to continue efforts working with the EMN on improving the regulatory framework for microcredit provision in Croatia. This work continued both in Croatia and at the second EMN LER-WG meeting in June in Stockholm, where the tentative action plan was developed and part of the required resources were identified.

Next Steps

An action plan was developed in order to coordinate the stakeholders' lobbying efforts and resources towards improving the legal and regulatory framework for microcredit provision in Croatia. The main activities planned for the following months are:

- ➔ Analysis of the current legal framework for microcredit provision in Croatia and identification of major gaps and compliance with the European legal framework, especially the European Code of Good Conduct for Microcredit Provision.
- ➔ Mapping of the stakeholders and sponsors of the legal framework initiative in Croatia to determine and quantify their involvement and contribution to the MF legal initiative (found in annex 1 - the list of main stakeholders of the sector, contact person and contact information).
- ➔ Drafting proposals for amendments and new regulation aimed to create an enabling legal framework for MF in Croatia and identify the key promoter/sponsor of the legal initiative.
- ➔ Develop lobbying strategy for the promotion of the new/amended legal framework and gather the resources needed to implement. This consists of the action plan implementation and achievement of secondary objectives as presented in annex 2 (attached), which summarizes the description of the main activities and the estimated time frame, methods and tools, and key messages aimed to achieve the overall objective, an enabling legal framework for micro-finance provision in Croatia.

Conclusions

The mapping exercise for the Croatia was developed with the assistance of the EMN's Working Group on Legal Environment and Regulation (LER), aiming to identify the key stakeholders of the microfinance sector, map their interest and capacity in lobbying for the creation of an enabling legal framework, and contribute to the development of an efficient and effective microfinance sector on Croatia capable of serving un-bankable entrepreneurs.

Improving the current legal framework for microcredit provision in Croatia and identifying the major gaps and compliance with the European legal framework, especially the European Code of Good Conduct for Microcredit Provision, will facilitate the creation of an enabling legal framework for MF in Croatia and to the socio-economic development of the country within the European Union context.

The DEMOS initiative uniting key stakeholders of the Croatian MF sector around promoting the improvement of the legal framework for microcredit provision will continue to be supported during the process by EMN as the main European MF network advocating among the decision-makers at European level for regulatory changes that enable growth and consolidation within the microfinance sector.

Acknowledgements to the members of the Legal Environment and Regulation Working Group (LER WG) 2013 for their active contribution:

- ➔ **DEMOS CROATIA, Croatia**, represented by **Mr Daniel GIES** and **M Josip BORZIC**
- ➔ **EUROM Consultancy and Studies SRL, Romania**, represented by **Ms Maria DOICIU**
- ➔ **FEJER ENTERPRISE AGENCY, Hungary**, represented by **Mr Tibor SZEKFU**
- ➔ **ICO FOUNDATION, Spain**, represented by **Mr Jaime Manuel DURAN NAVARRO**
- ➔ **MICRO DEVELOPMENT, Serbia**, represented by **Ms Milena GOJKOVIC**
- ➔ **NEEM, Sweden**, represented by **Ms Fatma MOHAMUD**
- ➔ **UNCAR, Romania**, represented by **Ms Ana Maria TOMA**

For specific questions about the Croatian microfinance sector, please contact:

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Annex 1

Contacts of the key stakeholders on the Microfinance sector in Croatia

	→ Key Stakeholder of the MF Sector	→ Address	→ Contact person	→ Telephone, fax, e-mail
1	Ministry of Finance	Katančićeva 5, Zagreb	Maroje Lang - Deputy Minister	Tel: 01/ 4591 479, Fax:01/4591 248, lucijana.poplasen@mfin.hr
2	Ministry of Economy	Ulica grada Vukovara 78, Zagreb	Ivan Vrdoljak - Minister	Tel. 01/6106-111, Fax.01/6109 110, ministar@mingo.hr
3	Ministry of Entrepreneurship and Crafts	Ulica grada Vukovara 78, Zagreb	Gordan Maras - Minister	Tel: 01/ 01/610 65 48, 610 67 39, Fax:01/610 69 21, pitanja@minpo.hr
4	Ministry of Regional Development and EU Funds	Račkoga 6, 10 000 Zagreb	Prof. Dr. Sc. Branko Grčić - Deputy Prime Minister and Minister, Valerija Smolčić - Administrative Secretary	Tel: 01/ 640 06 60, Fax: 01/640 06 44, valerija.smolcic@mrrfeu.hr
5	Ministry of Justice	Ulica grada Vukovara 49, Zagreb	Orsat Miljenić - Minister, Mirna Pereš Norac - Secretary	Tel: 01/ 371 45 00, Fax: 01/ 371 47 07, ministar@pravosudje.hr
6	Croatian National Bank	Trg hrvatskih velikana 3, Zagreb	Prof. Dr. Sc. Boris Vujčić - Governor	Tel: 01/ 456 47 81, Fax: 01/ 455 05 98, ured.guvernera@hnb.hr
7	Croatian Bank for Reconstruction and Development	Strossmayerov trg 9, Zagreb	Anton Kovačev - CEO	Tel: 01/ 4591 666, Fax: 01/ 4591 721, hbor@hbor.hr
8	European Bank for Reconstruction and Development	Miramarska 23/3, Zagreb	Vedrana Jelušić Kašić - Director	Tel: 01/ 600 03 10, Fax: 01/ 619 72 18, Milicici@ebrd.com
9	The World Bank	Radnička cesta 80/IX, Zagreb	Hongjoo J. Hahm - Country Manager, Croatia and Slovenia	Tel: 01/ 235 72 30, vfrajtic@worldbank.org
10	Croatian Banking Association	Centar Kaptol, Nova Ves 17, Zagreb	Zoran Bohaček - Director	Tel: 01/ 486 00 80, Fax: 01/ 486 00 81, info@hub.hr
11	Croatian Chamber of Economy	Rooseveltov trg 2, Zagreb	Nadan Vidošević - President	Tel: 01/ 456 17 12, Fax: 01/482 83 65, predsjednik@hgk.hr
12	Croatian Employers' Association	Pavla Hatza 12, Zagreb	Davor Majetić - Director General	Tel: 01/ 489 75 51, Fax: 01/ 489 75 92, dubravka.oreskovic@hup.hr (Secretary)
13	Croatian Chamber of Trades and Crafts	Ilica 49/II, p.p.166, Zagreb	Dragutin Ranogajec - President	Tel: 01/ 480 66 66, Fax: 01/ 480 66 76, ured.predsjednika@hok.hr
14	Croatian Cooperative Association	Amruševa 8/1, Zagreb	Vedrana Stecca - President	Tel: 487 00 53, Fax: 01/ 00 55, vedrana.stecca@hsz.t-com.hr
15	Croatian Employment Service	Središnji ured, Radnička cesta 1, Zagreb	Ankica Paun Jarallah - Manager	Tel: 01/ 612 60 00, hzz@hzz.hr , ravnateljica@hzz.hr
16	Croatian Trade Union Association	Trg kralja Petra Krešimira IV 2, Zagreb	Ozren Matijašević - President	Tel: 01/ 465 56 22; 01/ 465 56 88, Fax: 01/ 465 50 09, ozren.matijasevic@hus.hr

➤ Key Stakeholder of the MF Sector	➤ Address	➤ Contact person	➤ Telephone, fax, e-mail
17 Croatian Association of Credit Union	Zagrebačka avenija 100, Zagreb	Željka Pirija Benaković - President	Tel: 01/ 388 05 88, Fax: 01/ 388 05 45, huku@hukreditneunije.hr
18 Association of Credit Unions of Croatia	Draškovičeva 49, Zagreb	Krešimir Ivković - President	Tel: 01/ 492 29 30, kresimir.ivkovic@sabor.hr
19 DEMOS Savings and Loan Coop	Trg Josipa Broza 4, Karlovac	Josip Borzić - Director	Tel: 047/ 615 827, Cell: 091/ 411 99 62, borzic@demos-skz.hr

Annex 2

Timeline and Further Activities

	➤ Specific Objectives	➤ Activities	➤ Timeframe/ Duration	➤ Target (Who are we addressing?)	➤ Message (Which message do we want to convey?)	➤ Methods/Tools/ Approach (How convey the message?)
1	To determine the compliance of the current legal framework in Croatia with the ECGC	<ul style="list-style-type: none"> ➤ Analysis of the existing legal framework for MF in Croatia ➤ Primary legislation ➤ Secondary legislation ➤ Analysis of existing legal framework's compliance with the EU regulations (ECGC) ➤ Analysis of the legal framework for MF provision in the EU countries ➤ Draft the report on the legal gaps identified 	2 quarters January - June 2014	Existing MF providers in Croatia Policy makers	Compliance with the ECGC for MFP is a quality standard that applies to all EU MF providers. Access to the EU funds for MF is subject to compliance with the ECGC	Assessments of the legal framework Promotion of the ECGC to the key policy makers, Meetings with the key policy - makers
2	To identify the sponsors of the legal initiative and the resources needed to promote it	<ul style="list-style-type: none"> ➤ Mapping of the stakeholders and sponsors of the legal framework initiative in Croatia ➤ Identify StH and Sponsors of the MF legal initiative: Gov. representatives, MF representatives, EMN/EC, etc. ➤ Organize workshop with the StH and Sponsors of the legal initiative ➤ Present the report on the Legal Gaps Identified ➤ Quantify StH involvement and contribution to the MF legal initiative 	1 quarter June - August 2014	Existing MF providers in Croatia Policy makers EMN/EC	Without a coherent and enabling legal framework for MF provision, the access to financial resources of underserved entrepreneurs will remain among the most difficult in the region. The EU funds for MF available during 2014-2020 will not be used.	Workshop with the participation of the key stakeholders of the MF sector and the policy makers in Croatia

➤ Specific Objectives	➤ Activities	➤ Timeframe/ Duration	➤ Target (Who are we addressing?)	➤ Message (Which message do we want to convey?)	➤ Methods/Tools/ Approach (How convey the message?)
<p>3 To draft the new law/ amendments to the legal framework for MF provision in Croatia</p>	<ul style="list-style-type: none"> ➤ Draft proposals for amendments, new regulation aimed to create an enabling legal framework for MF in Croatia ➤ Present the proposals for new law/amendments 	<p>1 quarter August - November</p>	<p>Policy - Makers</p>	<p>The new/ improved legal framework will enable entrepreneurship development and growth to underserved entrepreneurs</p>	<p>Individual meetings with policy makers</p>
<p>4 To promote the legal initiative to the policy makers and follow up during the approval process.</p>	<ul style="list-style-type: none"> ➤ Lobby for the promotion of the legal initiative 	<p>2014 - 2015</p>	<p>Policy makers Beneficiaries of the MF services Key stakeholders of the sector</p>	<p>The legal framework enables entrepreneurship to underserved entrepreneurs</p> <p>The new legal framework will contribute to the sustainable development of the MF sector in Croatia able to access the EU funds for MF</p>	<p>Individual meetings with policy makers</p> <p>Presentations of the legal initiative to the endorsing relevant ministries and in the parliament commissions</p>