Kiútprogram, Hungary

This case study presents an integrated project that supported Roma people in business creation. The case study discusses the objectives and rationale for this approach, as well as the evolution of activities and the reasons for the changes in the approach. The project's impact is also presented. The challenges faced in implementation are discussed along with the conditions for transfer.

Objectives

Kiútprogram ran from 2010 to 2012. Its main objective was to promote social mobility and the integration of disadvantaged people in disadvantaged areas by enabling them to become self-employed by establishing and registering a small business. In addition, the project could also be accessed by those looking to convert informal business activities into legal enterprises. The scheme provided microcredit and supplementary business support services (e.g. mentoring, training) to support business creation. The target group was people living in poverty. It targeted explicitly, but not exclusively Roma women and men.

The founders and sponsors of the scheme defined the initiative as a "social microcredit scheme", indicating a balanced approach between the social cohesion and financial objectives. The scheme sought to improve social attitudes towards, and decrease discrimination against, vulnerable groups, such as Roma people.

Rationale

In Hungary, the share of self-employed among all employed people is significantly lower for Roma people (5%) than for the general population (15%). Further, within the Roma population across the Central Eastern European region, the Roma in Hungary have the lowest self-employment rate. On the other hand, 24% of the Hungarian Roma population would prefer to start a business over work as an employee (World Bank-UNDP, 2012).

In most countries with a considerable Roma minority, people from this group face severe challenges to (re-)enter the job market as self-employed. Research suggests that the main obstacles to business creation are limited access to financial services (including access to bank accounts and personal credit and loans) and limited experience in running a business. In addition, the Roma typically have a low level of education and very low levels of financial literacy (Molnár, 2012; World Bank-UNDP, 2012). The situation of the Roma people in Hungary is further exacerbated by strong negative stereotypes held in society and media (Bernáth-Messing, 2013). Prejudices persist, and enforcement of anti-discrimination legislation and administrative procedures to tackle ethnic discrimination is weak (Majtényi, 2009).

Kiútprogram aimed to address both market and government failures. It focused on remote, small regions of Hungary, where the level of business activity is low, public infrastructure is under-developed and business investments are far below the national average. Employment opportunities in these regions are typically limited to participation in public work programmes, which only offer fixed-term jobs (BI, 2011), or in the informal economy. This scheme was started to assist the Roma to meet the costs of starting a business and to encourage them to operate as a formal rather than informal business (Reszkető-Váradi, 2012; Molnár, 2012).

Activities

The Polgár Foundation for Opportunities, a Hungarian civil foundation, initiated the project in 2008 with an idea to adapt the Grameen model* to the Hungarian context. They commissioned a feasibility study, which consisted of field work that assessed the needs for such a scheme. In September 2009, following the feasibility study, the Foundation submitted a tender to the European Commission for a pilot project in microfinance. This application was based on the results of the preparatory research mapping the potential target regions and the local Roma communities' needs (Molnár, 2012; Szuhai, 2008). In March 2010, the European Commission helped launch the scheme as a European pilot project in microfinance for the period starting in October 2010 through June 2012. The Polgár Foundation was a co-sponsor.

According to Hungarian financial legislation, the disbursement of loan products can only be issued via financial institutions. Consequently, the Raiffeisen Bank became the financial managing partner of the project. The bank issued the loans and managed expenditures and losses within the framework of its corporate social responsibility scheme. The bank also offered savings accounts to clients and provided training to bank staff members in the regionally designated local branches to help them work with this client base.

The *Kiútprogram* Microcredit Initiative Non-profit Ltd. (i.e. the Managing Company) was established in September 2009. The Managing Company was in charge of the operation of the scheme, including training and co-ordinating the field workers, screening and training clients, delivering supplemental business development services and managing the loan contracts in partnership with the Raiffeisen Bank. The World Bank and the United Nations Development Programme (UNDP) supported the project with technical expertise in monitoring; i.e. the design of the monitoring database, and the collection and analysis of the monitoring data.

Field workers were the key actors in the delivery of the scheme's services. They were responsible for mapping and screening the potential settlements and participants, providing the training and individual business supports at local level, facilitating and supporting the preparation of individual business plans, and facilitating the operation of loan groups. With the progress of the implementation, they were also the key scheme agents in charge of monitoring the small business activities, organising the loan groups sessions post-disbursement and early signalling to the bank any potential future non-repayment or any other emergency. Most of the field workers were trained in social work

* The Grameen model was developed by Prof. Mohammed Yunus in Bangladesh. It follows a methodology where a microfinance institution is created in a village that caters to 15 to 20 other villages. The microfinance institution grants joint-responsibility loans to self-formed groups of about five borrowers (as in the solidarity group model). The loans are issued in waves; the first members get their loans, and then the next – if the first members have repaid their due – and so on. One mechanism to improve repayment is peer pressure within the group (OECD, 2015).

and were selected based on their work experience. All the field workers underwent a month-long training module before starting any field work.

Clients were recruited from regions with less than 60% of Hungary's median household income. The scheme prioritised women, however only 40% of the applicants and 48% of the clients were female. Interviews with clients – although not based on a representative sample – suggest that official numbers might over-report women's participation since many husbands or partners were the true business operator (World Bank-UNDP, 2012).

The selection process had two steps. First, the field workers screened the potential settlements. In the period 2010-12, the field workers visited 202 settlements in order to make public announcements about the scheme and to organise local community meetings where information on the microfinance scheme and the supplementary business services was shared. When communities showed a high level of interest in the scheme, field workers then visited families to assess the economic and social conditions of the potential participants on site. They also completed the intake questionnaire with the families during these visits to collect basic information about the applicants and their households.

At this stage of the selection process, loan groups of 8 or 9 candidates were formed. Group meetings were organised and field workers explored the past business experiences of the group members. The group had to select a leader and to approve the group rules. Potential candidates also had to meet a number of selection criteria (e.g. have no unpaid taxes) and also had to create a simple but realistic draft business plan. The Credit Committee operated by the Managing Company evaluated the individual application packages, which included the on-site questionnaire, an evaluation by the field worker, the draft business plan, and an individual self-scoring, and made the final decision in consultation with the field worker.

Following the Grameen model, this scheme was based on group lending. Loan groups served as a substitute for the lack of collateral and as a forum for sharing experiences and mutual learning. Group dynamics and operating rules were intended to enforce repayment since the group members received loans sequentially, and on the condition of no failure. The group leader was the last to receive their credit. Loans were provided according to 3 schedules: a loan of EUR 670 to repay over 6 months; a loan of EUR 1 670 to repay over 12 months; and a loan of EUR 3 330 to repay over 18 months.

Project development

It became clear in early 2011 that adjustments were necessary in the project design. During the Autumn of 2010, recruitment of clients took off much slower than expected. By the end of 2010, the scheme had 11 loan groups with about 70 participants involved, which was below the initial scheme target of 100 clients by the end of the first year. This also jeopardised the overall target of having 400 clients. In addition, the failure rate was extremely high: 80% of loans had late, or non-repayment.

During the first half of the second year, the following changes were introduced:

- *Enhanced screening of clients and shift in geographic targeting.* Field workers put greater emphasis on mapping credit history, business links and experience of both the potential clients and their family members. They also moved away from the most disadvantaged small regions. As a result, potential clients who had prior business experience or at least links to existing business networks became more likely successful candidates. It also resulted in slightly higher economic strata as a new target group.

- *Broadening the scope of supported business activities*. Due to client demand, agriculture was added as a possible sector to start business.
- *Enforcing repayment and group dynamics*. The scheme allowed the formation of loan groups with fewer than 5 members – a minimum threshold that was strictly enforced during the first period. Loan groups also increased their focus on developing business plans and introduced stricter evaluation criteria. The loan size was also decreased to an average amount and duration of EUR 1 832 and 43 weeks, and increased flexibility was provide to reschedule loans. This helped ensure that clients could pay even after the end of the first 6 months of business operation. In addition, loan groups received more support in accessing the state support scheme *Vállalkozóvá Válási Támogatás*, which was available for start-ups for the first 6 months of operation. Participation in this scheme allowed for the re-financing of tax and social security contributions (according to national regulations, self-employed people were required to pay taxes and social contributions based on the minimum wage level fixed for the given financial year – independently of their actual revenues).
- *Reinforcing management and improving the training of the field workers*. The scheme established a crisis committee to provide individual assistance to clients who were at risk of default, and hired new field workers with more experience in social work. Additional training was also provided to field workers in response to clients' feedback. The scheme also nominated regional co-ordinators to improve communication among the field staff and between the project office and the field workers.

Project financing

The European Union project "Pan-European Co-ordination of Roma Integration Methods – Roma Inclusion: Self-Employment and Microcredit" was the main financial source for the *Kiútprogram*. The overall budget of the project – including operational costs and loan portfolio – was EUR 1.4 million. The European Union project provided pre-financing (85%), and the remaining share was assured after the official closure of the project. The Hungarian government co-financed the project management costs (HUF 200 million, or approximately EUR 666 670) and other state supports (re-financing of tax and social security contributions) amounted to HUF 135 million (approximately EUR 450 000) during the project period. After the end of the pilot phase, the project follow-up activities and some of the local projects were financed by private sources, mainly the Polgár Foundation.

Challenges encountered

The scheme faced 3 principal challenges. The *first* was targeting appropriate clients and identifying those who had the potential to succeed in self-employment. The sustainability of any business activities in the most disadvantaged regions was challenged by limited regional market demand and business networks. Consequently, the *Kiútprogram* shifted its focus to "upmarket" clients, and to locations with better access to regional markets and existing business networks. However, this undermined the social objectives of the scheme.

The *second* challenge was to recruit the strong field workers who could simultaneously act as a personal mentor, a community worker, and a loan agent with relevant financial and business expertise. One option could have been to hire different people for different tasks, but the project budget did not allow for this. The turnover rate of the field workers was extremely high during the first operative year (i.e. approximately 90% of the field workers hired in the first months of the project implementation period left in the following year), indicating the difficulty of the job. The Managing Company launched 5 calls for field workers during the two-year project period.

Thirdly, new businesses need time to develop and gain a sustainable client base. This often takes more than one year. The *Kiútprogram* was able to develop a co-operation with the Hungarian public employment offices to guarantee access to the specific state aid scheme available for new entrepreneurs for the first 6 months of their operation but were unsuccessful at coming to a partnership agreement at the institutional level that could last more than 6 months. This created a challenge for participants who had to adhere to a weekly repayment schedule.

Impact

There is no *ex post* evaluation of this project. However, a comprehensive monitoring system was set up in partnership with the World Bank and the United Nations Development Program (UNDP). Monitoring data show that were 192 participants in total and 138 joined a loan group. Of these, 49 people received loans under these settings with an average loan of EUR 1 825 per person and an average duration of 52 weeks.

The project succeeded in reaching unemployed people (86% of applicants had been unemployed for more than one year before entry or was registered as inactive) and households with very low monthly income (median monthly household revenue was HUF 68 250, or approximately EUR 227). The share of applicants with secondary education or higher was very low (13%), and 87% of them lived in a rural area.

Businesses that received financing were either in agriculture and forestry (45%) or retail (55%). Based on the intake survey undertaken by the World Bank, 68% of the clients lacked the finances to start a business and 95% claimed that the main source of starting capital was the loan received through the project. These businesses generated, on average, monthly sales revenue of HUF 68 312 (approximately EUR 227). In May 2013, approximately one year after the official project closing, 45% of the businesses were still in operation.

Ex post monitoring suggests that women and those were active in community life before the project (i.e. taking part at least weekly in discussions and decisions of some kind of local community) were the most likely to repay according to the agreed repayment schedule (World Bank-UNDP 2012). These findings are in line with international experiences and underline the importance of local networks and personal relationships.

Further, monitoring studies emphasised the importance of a comprehensive approach in the project design, which is neglected by its label as a social microcredit scheme (World Bank-UNDP, 2012; Reszkető-Váradi, 2012). Both studies suggest that it would have been advantageous to have had a longer pilot period (i.e. at least 3 or 4 years) and that less ambitious outcome indicators could have led to the development of higher-quality business support services. They also note that more consideration should have been given to participants' exit strategies and a clear phasing-out of support.

Regarding cost-effectiveness, the World Bank-UNDP (2012) compares the *Kiútprogam* to public work programmes. They estimated similar monthly costs (EUR 2 010 per month per client), but it is noted that *Kiútprogram* might be more successful at improving clients' chances of becoming employed or self-employed.

Conditions for transfer

This project provides an example of how the most disadvantaged members of society can be supported through entrepreneurship. The experience provides many lessons for similar initiatives:

1. *Ensure strong field workers*. The field workers proved to be the key actors in the implementation phase. The *Kiútprogram* provides good lessons on the selection of field workers and the diversification of their tasks. The simultaneous roles of being social worker and loan agent and the complexity of the related services may turn out to be a barrier. It may therefore be necessary to differentiate the responsibilities and hire staff members specialised in these different roles separately.
2. *Utilise intensive outreach*. The scheme intends to assist disadvantaged groups in disadvantaged areas. The key to reaching this group so that it is aware of the available support is to go into the field and interact with them directly. This also has the advantage of identifying potential candidates and building trust between the field workers and the clients.
3. *Develop realistic targets*. This scheme had to make major adjustments during the pilot phase because it was clear that it was too ambitious and too selective. As a result, the profile of the target client changed and many of the social objectives were compromised. It is important to undertake an *ex ante* evaluation to ensure that the project design matches the objectives and targets.
4. *Ensure that loans are appropriate*. The size of the loan offered should be tailored to the business environment and the needs of participants' businesses. This implies higher start-up capital in European countries than in the developing country context where this type of approach originated.

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