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Social Enterprises over Microfinance Institutions: The Challenges of Governance and Management

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Abstract : Upon the end of the vicious war in former Yugoslavia in 1995, international development community widely promoted microfinance as the key development framework to eradicate poverty, create jobs, increase income. Widespread claims were made that microfinance institutions would play vital role in creating a bedrock for sustainable 'bottom-up' economic development trajectory, thus, helping newly formed states to find proper way from economic post-war depression. This uplifting neoliberal narrative has no empirical support in the Republic of Croatia. Firstly, the type of enterprises created via microfinance sector are small, unskilled, labor intensive, no technology and with huge debt burden. This results in extremely high failure rates of microenterprises and poor individuals plunging into even deeper poverty, acute indebtedness and social marginalization. Secondly, evidence shows that microcredit is exact reflection of dangerous and destructive sub-prime lending model with 'boom-to-bust' scenarios in which benefits are solely extracted by the tiny financial and political elite working around the microfinance sector. We argue that microcredit providers are not proper financial structures through which developing countries should look way out of underdevelopment and poverty. In order to achieve sustainable long-term growth goals, public policy needs to focus on creating, supporting and facilitating the small and mid-size enterprises development. These enterprises should be technically sophisticated, capable of creating new capabilities and innovations, with managerial expertise (skills formation) and inter-connected with other organizations (i.e. clusters, networks, supply chains, etc.). Evidence from South-East Europe suggest that such structures are not created via microfinance model but can be fostered through various forms of social enterprises. Various legal entities may operate as social enterprises: limited liability private company, limited liability public company, cooperative, associations, foundations, institutions, Mutual Insurances and Credit union. Our main hypothesis is that cooperatives are potential agents of social and economic transformation and community development in the region. Financial cooperatives are structures that can foster more efficient allocation of financial resources involving deeper democratic arrangements and more socially just outcomes. In Croatia, pioneers of the first social enterprises were civil society organizations whilst forming a separated legal entity. (i.e. cooperatives, associations, commercial companies working on the principles of returning the investment to the founder). Ever since 1995 cooperatives in Croatia have not grown by pursuing their own internal growth but mostly by relying on external financial support. The greater part of today's registered cooperatives tend to be agricultural (39%), followed by war veterans cooperatives (38%) and others. There are no financial cooperatives in Croatia. Due to the above mentioned we look at the historical developments and the prevailing social enterprises forms and discuss their advantages and disadvantages as potential agents for social and economic transformation and community development in the region. There is an evident lack of understanding of this business model and of its potential for social and economic development followed by an unfavorable institutional environment. Thus, we discuss the role of governance and management in the formation of social enterprises in Croatia, stressing the challenges for the governance of the country's social enterprise movement.

Keywords : financial cooperatives, governance and management models, microfinance institutions, social enterprises
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