Financial cooperatives for sustainable local economic and social development

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The last 30 years or so has seen the commercial or 'new wave' microfinance model rise to dominate the poverty reduction agenda in both developing and transition countries alike. Initially inspired by the Grameen Bank model that emerged in Bangladesh in the 1970s, but later refined to incorporate more fully standard neoliberal commercialization imperatives, the microfinance model is now the most visible poverty reduction strategy around. Nevertheless, even its strongest supporters agree that it still remains moot as to whether it actually possesses the required 'transformative capacity' to secure permanent poverty reduction associated with genuinely sustainable national, regional and local economic and social development.

This article looks at a local financial systems model arising in Western European practice that, in contrast to the commercial microfinance model, is unequivocally associated with sustainable economic and social development and growth, and thus also sustainable poverty reduction. The author argues that this 'integrated cooperative financial systems model' should have had, and should still have today, enormous implications for developing and transition countries (still) seeking to construct local financial institutions that are capable of establishing genuinely equitable and sustainable local economic and social development trajectories.

THE RECENT (OCTOBER 2006) AWARD of the Nobel Peace Prize jointly to the Grameen Bank and to its founder, Muhammad Yunus, is but the latest twist in an almost unprecedented decade-long blitz of hype and publicity surrounding the commercial microfinance model. The international development community is in almost universal agreement that commercial microfinance is 'a very good thing' – hence the Microcredit Summit campaign beginning in 1997 and the UN designating 2005 as the 'International Year of Microcredit'. While narrow political/ideological motives clearly lie behind much of the rich nations' adulation of and support for the commercial microfinance model (for example, see Weber, 2006), it is nevertheless the case that very much is still expected of it on the ground in both developing and transition economies.

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Yet, notwithstanding the microfinance model's now very high profile in the international development community, in key western governments and in academia, there still remains, strange as it may seem, real uncertainty regarding its longer term sustainable development impact. Even if some short-run poverty reduction impacts are pretty much agreed upon,

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the fact remains that we are still not at all sure if such impacts are sustainable into the longer run. It may even be the case that the commercial microfinance model actually destroys the chances of sustainable development in the longer run.

Most microfinance is channelled into informal, low-skills, under-capitalized and largely no-growth micro-ventures

Uncertainty as to the real longer-term impact of the microfinance model arises, I would argue, principally because of issues on the lending/investment side. A key facet of the commercial microfinance model is that the overwhelming bulk of microfinance is everywhere very consistently channelled into rafts of informal, no-technology, low-skills, low productivity, under-capitalized and, thus, largely no-growth micro-ventures. And the problem is that this basic programmatic outcome sits very uneasily alongside the huge weight of empirical evidence from a wide range of countries, regions and historical contexts that such a 'shallow' informal enterprise structure is a very unsuitable foundation in practise upon which to construct a sustainable economic growth and development trajectory. Some international development agencies, for example the United Nations Conference on Trade and Development (UNCTAD) (2003), have been issuing warnings in this direction for some years. But it seems that the urgent need everywhere is instead simply to create large numbers of new jobs – even if unregistered, poorly paid, insecure, undignified and dangerous, and ultimately unable to promote sustainable growth – in order to as rapidly as possible absorb the growing numbers of poor, excluded, unemployed, under-employed and marginalized that constitute the growing downside of globalization today.

Do as we say, not as we did. Moreover, the rich developed western economies now proffering microfinance advice worldwide certainly did not achieve their own poverty reduction and sustainable economic development successes because of the microfinance model, but effectively thanks to its antithesis. As both Linda Weiss (1998) and Ha-Joon Chang (2002) have pointed out, the developed western countries praise the pure market model (neoliberalism) today, but they scrupulously avoid to mention to their developing and transition country 'students' that their own poverty reduction successes were achieved thanks largely to something completely different – that is, to various forms of state planning, coordinated investment strategies, socializing of private sector risk, extensive regulation, and comprehensive industrial policies built around 'infant-industry' tariff protection, low-cost credit and vastly subsidized technology and innovation support structures. The same essentially goes for the rapid poverty reduction and sustainable development achieved in many (then and still) developing countries, notably Taiwan and South Korea from the 1960s onwards, as Wade (1990) and Amsden (1989) vividly document, and more recently in Brazil, China, India, Malaysia, Thailand and Vietnam, as both Taylor (1994) and Lall (1996) have pointed out.

The West's own poverty reduction successes were achieved thanks largely to something completely different

Put simply, the key sustainable poverty reduction and local economic development and growth triggers – technology upgrading, cumulative investment, reaping scale and scope economies, incorporating innovation, integration into horizontal and vertical efficiency-enhancing linkages, and promoting education and training – simply do not factor into the world of commercial microfinance. In fact, as Bateman (forthcoming) documents with regard to the supposedly 'best practice' case of Bosnia and Herzegovina, the commercial microfinance model can ensure that such crucial local economic development triggers are routinely *undermined* or, worse, completely *destroyed.* The rub is, therefore, that the commercial microfinance model may well be able to partially address the immediate issue of poverty, but it only achieves this feat by establishing a set of local 'initial conditions' that might permanently lock in under-development and generalized poverty. The immediate poverty reduction gains registered by the commercial microfinance model thus come at a very high price indeed.

These real concerns, among others, then beg an obvious question: are there any practical local financial systems models that are more closely associated with having achieved sustainable local economic and social development, and, if so, what can we learn from them? This is the subject of this article.

The background

It is very often forgotten today, or perhaps deliberately ignored, that after 1945 several Western European regions established a broadly similar local financial systems model that was pivotal in facilitating sustainable local/regional economic and social development. Two regions in particular stand out in this regard: the region of Emilia-Romagna in central-northern Italy and the Basque region of northern Spain. Both regions were extreme economic, political, social and cultural casualties of World War II. Thereafter, both regions became victims of various cold war-related ideological and political battles, as well as a good dose (in northern Spain) of residual inter-ethnic acrimony. Notwithstanding, both regions were able to establish a broadly similar local financial model, an 'integrated cooperative local financial systems model' – let's call it the 'IC model' – that proved to be highly successful in reconstructing both regions, and then equally successful in maintaining an upward growth and equitable development curve right up to the present day. Crucially, the IC model that emerged in Spain and Italy enjoyed its most important success by helping to establish, expand and consolidate a flourishing cooperative sector, which in both cases eventually became the dominant feature of the regional economy. Overall, the two regions in question are now probably the EU's best examples of sustainable and equitable regional economic and social development.

The integrated cooperative model proved to be highly successful in reconstructing both regions

Emilia-Romagna

Consider first the region of Emilia-Romagna in central-northern Italy. Heady with their war-time victory against both local and Nazi Fascist forces, and then given an electoral mandate by the region's population, the newly elected communist-led government in Emilia-Romagna quickly moved to design and construct its own regional/local financial systems model. The core concern was to somehow promote fair and dignified employment opportunities, equity and social justice, and social and inter-class solidarity. This development philosophy eventually came to be known as the 'consensus-driven' approach. Centrally it meant that the painful reconstruction period should lead to benefits for all, and not just for the most aggressive, entrepreneurial or well-connected individuals.

The reconstruction was planned to lead to benefits for all

The practical expression of this 'consensus-driven' philosophy was an unorthodox regional economic strategy involving a major role for new and existing community-based and cooperative financial institutions, which would in turn be expected to offer particularly favourable support for all manner of cooperative enterprises, such as employee, agricultural, marketing and consumer cooperatives. The new and existing cooperatives supported were all expected to accord to the rules for genuine member-owned and controlled cooperatives established by the International

Microenterprises were expected to adopt dignified working conditions and social benefits for employees

Cooperative Alliance (ICA). Traditional privately owned microenterprises were also offered significant support, so long as they indicated their willingness to accept the new parameters relating to dignified working conditions, social benefits, trade union representation and so on. The new regional/local integrated cooperative financial systems model, the IC model, was thus designed to respond to the need to gradually reconstruct and develop the local micro- and small enterprise sector in terms of new employment relations (secure, dignified, quality jobs, not exploitation), new ownership structures (a preference for cooperatives), technologies deployed (more use of modern technologies, 'state-of-the-art' if possible) and interconnections (encourage efficiency-enhancing horizontal and vertical linkages).

Development-focused institutions were critical. Several financial institutional innovations were important in getting things moving. First, the previously strong cooperative banking sector was helped back on its feet and it quickly began to restore its financial strength, pulling in savings from all across the community. The main cooperative bank in Emilia-Romagna – Cooperbanca – had branches right across the region and it quickly became a mainstay of lending to small and medium enterprises (SMEs) and, particularly, to the cooperative sector. The smaller cooperative banks in Emilia-Romagna were also helped to recover and were quickly able to provide additional support to both cooperatives and individual micro-entrepreneurs. Second, starting in 1947, a very significant proportion of the microenterprises in Emilia-Romagna were helped to tap into Artisanal Funds established and capitalized by the central government in Rome, but largely managed and accessed regionally. Weiss (1988) shows how these Artisanal Funds were very successful in providing long-term (10 year) low-interest loans for machinery purchase and workshop modernization. Third, also in 1947, a network of full and part publicly owned Special Credit Institutes (SCIs) was established across Italy to specialize in providing low-cost medium- to longer-term credit to small and medium industrial and relatively technology-intensive enterprises. The SCIs established in Emilia-Romagna were particularly proactive, transparent and well managed, with the result that a disproportionate amount of the central funding available was channelled to the SME population under their jurisdiction (recent changes to the banking structure in Italy have removed the SCIs as a separate category of financial institution).

The Special Credit Institutes specialized in medium- to longer-term credit for more technology-intensive enterprises

In other areas, however, the Italian central government was also very supportive of the activities underway in the central-northern regions. For example, in 1947 it established a special branch of the Banco Nazionale del Lavorio dedicated to providing financial support packages for cooperatives, greatly increasing its funding in 1951 and then again in 1962. The central-northern regions could and did access this funding easily. Also in 1947 the central government passed the 'Basevi Law' that granted a range of fiscal incentives to genuine cooperatives in order to encourage greater reinvestment of funds, which the central-northern regions also utilized probably more than other Italian regions.

Success of the cooperative sector helped to accelerate new cooperative development. These initial institutional developments created a real momentum for sustainable development in the central-northern regions, but especially in Emilia-Romagna. Changes were made to the region's evolving IC model over the years, but it remained an extremely focused and long-term-oriented financial structure. A reflection of the ongoing success of the IC model came in 1992 with the establishment of Coopfond. Coopfond was established following a new law that stipulated that all cooperatives – many now very successful and financially strong – must in future contribute 3 per cent of their profit into developing new and expanding existing cooperatives. This support was granted in return for the continuation and extension of various tax and other benefits attributable to genuine cooperatives. It quickly became an important new source of development funds for the cooperative sector, among other things partially replacing the financial support that had been previously available through the now very large and successful cooperative banks (which were increasingly being forced to focus on larger national-level enterprise development and infrastructure projects).

Coopfund quickly became an important new source of development funds for the cooperative sector

As well as qualifying for most of the above state-coordinated programmes of enterprise support, the assigned special importance of the cooperative sector in central-northern Italy meant that it was given further important encouragement by its own dedicated institutional support structure (albeit often financed by regional and local governments). For example, Legacoop, Italy's largest left-oriented cooperative membership body, became especially active in supporting its member cooperatives to grow and new ones to get started. As its financial strength rose in line with the growth of the cooperative population, Legacoop was able to branch out into many new development-related activities, such as assisting in the conversion of failing investor-driven companies into cooperatives and the establishment of venture funds to support new cooperatives.

In 1969, Legacoop consolidated its growing and varied programmes of financial support into Fincooper, a dedicated financial support institution initially backed by 200 of the most successful cooperatives. By the end of the 1990s, as emphasized by Piero Ammirato (1996), Fincooper had strategically invested the deposits of more than 2,000 member cooperatives into a wide range of cooperative and investor-driven companies of importance to the cooperative movement. After 1992, when the state added to its financial support for the cooperative sector with the Coopfond initiative, Legacoop decided to establish its own version of the Coopfond with 14 regional offices to utilize these new mandated funds to support the cooperative sector. Between 1994 and 2001, Logue (2005) reports that the Legacoop-affiliated Coopfond supported 109 new cooperatives into operation using $48 million of equity funding and $17 million of loans, in the process creating 4,640 new jobs. Similar support provided to existing cooperatives with growth potential deployed $52 million of funding to create 2,690 new jobs.

Cooperative economic success allied to the highest levels of social capital in the EU. The combination of external state support and growing internal cooperative membership body-driven activity helped the cooperative movement and ethos to grow very fast and strong in Emilia-Romagna. Importantly, as the wider investor-driven enterprise sector in Italy endured a very difficult time during the 1980s and 1990s, the cooperative sector was, in stark contrast, able to flourish as never before, increasingly by the conversion of a growing number of failed investor-driven enterprises into cooperatives. By 2003, Emilia-Romagna had both the highest number of cooperatives in Italy and the highest proportion of economic activity – more than 40 per cent of its GDP – in the cooperative sector. As a result of the intense cooperative sector activity, and also the equally famous 'industrial districts' phenomenon, the regional capital city – Bologna – became the richest city in Italy, while once poor and under-developed Emilia-Romagna became the second richest region in Italy and

More than 40 per cent of Emilia Romagna' GDP was in the cooperative sector

Social capital derived from the cooperatives is highly associated with quality of life

the 10th richest region in the EU. Perhaps most important of all, the region of Emilia-Romagna has regularly topped European quality of life surveys thanks to the very high levels of social capital generated through the emphasis upon the cooperative model. According to Stefano Zamagni of the University of Bologna, 'Social capital is highly associated with quality of life everywhere (and) it seems that the co-operatives' emphasis on fairness and respect contribute to the accumulation of social capital here' (quoted in Logue, 2005: 25).

Northern Spain

A very similar bottom-up dynamic has been evident in the Basque region in northern Spain since the mid-1950s, focused initially on the small town of Mondragón. Starting with a small cooperatively managed technical training school established by Don José Maria Arizmendiarrieta, a local parish priest, a group of the first students graduating were encouraged to seek to work cooperatively through a worker cooperative. A first worker cooperative, called Ulgor, was founded in 1956 in Mondragón, making stoves for the Spanish market. The initial financial resources required to underpin Ulgor were generated within the local community. Going from house to shop to small enterprise, the original founders were able to gather together promises of around $360,000, a huge sum for a very poor community at that time, in order to establish their cooperative factory initially meaning to employ no more than 20 people. The conclusion reached from this experience was that sustainable local growth would inevitably require a systematic mechanism both to generate local savings and, crucially, to ensure that such savings were wisely invested into new local industrial cooperatives.

A bank designed to develop the community, not simply to survive on the market. The result in 1959 was the Caja Laboral Popular (CLP) (Working Peoples' Bank), a secondary cooperative established by four of the earliest cooperatives. As Morrison (1991) records, this local financial vehicle was to prove quite central to the transformation of a limited and perhaps transitory experiment in local economic democracy into a major regional cooperative system. The CLP grew rapidly as savings were quick to be realized among the hard-working and thrifty local population. The key to the CLP's stunning success and its widespread popularity among the population, however, was not just that it could successfully mobilize local savings, but with how these savings were used once mobilized. The strength of the CLP lay in it rapidly developing an ability to efficiently recycle these valuable local resources into the expansion of sustainable industrial and technical services cooperatives in the locality. Historically, the large volume of savings mobilized in Mondragón had achieved very little indeed, most of it being reinvested locally into very small local businesses with no real growth potential. The cooperative projects coming to the CLP to obtain support, however, were all carefully evaluated on their individual economic merits and growth potential, their 'strategic fit' within the growing Mondragón group, and their adherence to Mondragón principles of cooperation and mutual support. Adhering to these basic developmental principles over the next 50 years meant that by 2005 the CLP had more than €12 billion of savings under its control and was successfully investing in enterprises (cooperative and investor-driven) right across Spain.

The cooperative projects applying for support were evaluated on their economic and growth potential

The model begins to be taken up by other poor regions in Spain. The Mondragón group quickly began to prove not just a success locally, but also an inspiration throughout the entire Basque region. Even more distant regions began to hear about the very positive Mondragón, later Basque, experience. For example, government officials from the very poor Autonomous Region of Valencia came to Mondragón in the 1970s to examine its institutions, and came away with ideas to replicate their core features back home. The significant cooperative-driven success they subsequently achieved in no small measure was due to the willingness to learn from the IC model and fashion their own financial, developmental and other institutions based on the same principles. Rising from almost nothing in the 1970s, by 2001 there were 123 agricultural cooperatives in the Valencia region, of which 100 were almost exclusively in the citrus industry producing nearly 1 million tons of citrus fruits per year. Exports in 2001 were more than €1 billion or around 60 per cent of the total citrus exports for all of Spain. The worker cooperative sector also began from more or less nothing but is now composed of more than 1,250 worker cooperatives with more than 22,000 members.

By 2001 there were 123 agricultural cooperatives in the Valencia region

In the 1990s, a restructuring process, forced largely by Bank of Spain regulatory pressure, repositioned the CLP as semi-independent of the operations of the Mondragón cooperatives. The CLP today generates savings from all across Spain, while its lending activities are also no longer confined to establishing and thenceforth supporting the Mondragón cooperatives. Through its Cooperative Development Department (Centro de Promocion Cooperativa), however, the CLP continues to provide technical and advisory services to large cooperatives, significant conversions to cooperatives and larger new start-up cooperative projects. It also continues to provide low interest loans to promising new and emerging cooperative projects right across Spain. In addition, it established a separate financial vehicle, MCC Investments, that provides special low-cost funds to medium to larger cooperatives.

The restructuring of the CLP also involved a possible relative decline in the level of financial and technical support provided to new small cooperatives in the Basque region, both start-ups and existing ones. The effects of this reduced focus upon the Basque region were muted, however, thanks to the coordination with local and regional government structures. Local and regional governments responded to the changes by taking steps to establish a number of new institutions to fill any impending 'funds gap'. One such new institution was Oinari (keystone), a mutual credit guarantee fund for cooperatives, which provides guarantees of up to €600,000 for new cooperative projects. Local governments also beefed up their own development funds earmarked for new and expanding cooperatives. At the same time, the various and now well-funded cooperative federations and sectoral associations in the Basque region also stepped in to provide affordable financial support for new cooperative start-ups and expansions.

Local governments also increased their development funds earmarked for new and expanding cooperatives

Economic and social success, and high levels of social capital. Very much as in Emilia-Romagna, the Basque region managed to weather the difficult 1980s and early 1990s world recession and went on to develop even faster than before. In the mid-1990s, the Mondragón cooperatives were comprehensively restructured, creating the overarching Mondragón Cooperative Corporation (MCC), composed of three divisions – distribution, financial and industrial. By 2006, the MCC had grown into a network of more than 120 inter-linked cooperatives, mainly industrial worker cooperatives. MCC currently employs nearly 80,000 full-time member-employees and is the seventh largest 'corporation' in Spain with a turnover in 2005 of around €12 billion. Also reflecting the very important outcome in Emilia-Romagna, the nature of the cooperative enterprise structure and its regional proliferation since 1956 has resulted in levels of social capital in the Basque country that are probably the highest in all of Spain.

Key lessons for developing and transition economies today?

The search for the precise reasons why and how both regions developed in the way that they did, and why so successfully, has spawned an enormous literature. However, one thing that is pretty much agreed upon is that in both Emilia-Romagna and in the Basque region a quite crucial sustainable development contribution was played by their similar IC models. The very successful IC model differs from the prevailing commercial microfinance model in a number of crucial respects.

There is no concern in microfinance regarding what type of microenterprise is being supported

Both savings and investment are crucial. In the commercial microfinance model, generally no concern is registered as to exactly what type of microenterprise is being supported or what might be the cumulative local development impact of the structure of microenterprises actually supported. Any individual microloan advanced must simply be repaid on time under the prevailing interest rate regime. Neoclassical economics maintains that this is the correct course to take and will ensure 'best use of funds'. Given that local savings mobilization is increasingly underpinning the operations of microfinance institutions everywhere, there is now even more concern with the financial operations, stability and sustainability of the microfinance institution.

Consider two examples of what happens in practice. Two of the most celebrated microfinance banks of recent years, Pro-Credit in Kosovo and ACLEDA in Cambodia, are rightly lauded for their professionalism and profitability. However, both banks do not seek to favour those particular micro-ventures embodying the most long-run sustainable development and poverty reduction potential, even though such micro-ventures are readily identifiable in both regions/countries. In Kosovo, one of the best (if not only) sustainable development potentials lies with invigorating the many small-scale farms and intermediate institutions (for example, agricultural cooperatives) wishing to service the local market and to replace imports (80–90 per cent of food items are imported into Kosovo). With large-scale industry effectively dead, and the petty services sector (shops, kiosks, shuttle trading and so on) already vastly overcrowded, this previously net agricultural exporting region urgently needs to help its small semi-commercial farmers integrate into the local market. In Cambodia, many millions of desperately poor rice farmers wish to improve productivity and farm-level earnings in an enormously important (three out of every five Cambodian families depend on their land and rice farming for a living) but very poorly rewarding sector. However, most Cambodian farmers remain trapped in vicious poverty because they cannot escape the traditional 'cycle of dependency' whereby they take an advance of rice seed, or a cash advance to purchase it, but must then give up most of any harvest in order to repay the advance.

Agriculture is often ignored by MFIs

Meanwhile, both Pro-Credit and ACLEDA prefer to generate higher and safer returns by focusing on supporting the local trade sector, in the process creating and adding to a 'bazaar economy' of quite impressive proportions but that contains almost no inherent sustainable development potential whatsoever. (ProCredit's business loan portfolio in mid-2002 involved loans to microenterprises and SMEs engaged in the following sectors: 66 per cent trade, 20 per cent services, 12 per cent production and

2 per cent agriculture. In 2005, more than 70 per cent of the loans advanced by ACLEDA went into the trade sector, with only 3 per cent of its disbursed loans going into agriculture). Such microfinance ‘cathedrals in the desert’ are becoming increasingly commonplace in both developing and transition economies alike.

Under the IC model, concern for efficient savings mobilization was matched by concern for social objectives

A fundamental aspect of the ‘best practice’ derived from the IC model in both Spain and Italy, however, is that concern for efficient savings mobilization simply must be matched by an equal concern for the local outcome generated via enterprise development using those same local financial resources. These combined goals were made possible because both IC models involve financial institutions owned and controlled by the community and thus infused with a clear set of social and community development objectives. Accordingly, pretty much equal care and patience went into professionally managing the local savings mobilization side and thenceforth identifying and patiently supporting cooperative and other business ventures that would make the very best use of local savings from the point of view of the community. The eventual economic and social impact of those cooperative and other enterprises supported and succeeding was, as expected, very much higher than would have likely been the case under a much more commercially driven process of client selection.

In the Basque country, a major part of the CLP's activity was to identify potentially sustainable business areas within the expanding cooperative group and in the wider Basque region, and locate these ideas either within existing cooperatives that could then expand, or establish entirely new cooperatives up to the task. As a sort of ‘social venture capitalist', the CLP was willing to support new cooperatives only if they had a business plan strongly suggesting long-term success and if they could prove that they would contribute to the longer-term development of the cooperative group and the local economy (for example, creating well-paid, secure local jobs). With both workers and owners benefiting from a share of the profits, the prospective workforce was also very much interested in becoming involved with a cooperative that had a good commercial future. In Emilia-Romagna, too, the new cooperative and investor-driven ventures supported by the cooperative banks, SCIs and Legacoop-affiliated financial bodies were all expected to prove commercial viability and their broad appropriateness within their social objectives framework established by the regional government.

With both workers and owners sharing in the profits, the workforce wanted to be involved with a cooperative that had a good commercial future

Development promotion cannot be configured as a commercial activity. In the commercial microfinance model, while established with social objectives in mind – immediate poverty alleviation – the worldwide trend is for microfinance institutions to prioritize their own financial sustainability, effectively becoming commercial institutions themselves. Such a move is justified on the basis that the resulting wider availability of microfinance is the best thing for the community because ‘more microfinance equals more development'.

In the IC model, however, there is specific recognition that promoting sustainable development is simply not a commercial activity. On top of a general requirement that they efficiently use whatever funds were placed at their disposal (local savings, subsidies and so on), the IC models in both Spain and Italy were established with the financial resources ‘to do the job'. In both regional examples, the social objectives took precedence over the conventional individual and short-run motivations that are typically important within the commercial microfinance model today. Rather than saving in order to support your local community, in the commercial

The local populations managed to save so much in the first place precisely because of the social objectives

microfinance model savers are encouraged by the highest possible interest rates, which are generally secured, as we have adumbrated above, by almost exclusively working with the most immediately profitable local microenterprises rather than those with the most long-term potential to develop. Crucially, in both Emilia-Romagna and in the Basque region, the main reason why the exhausted and impoverished local populations were willing to save so much in the first place was precisely because of the social objectives embodied in their respective IC models.

Cooperatives are a 'better' economic, social and cultural enterprise format to support. In the commercial microfinance model, the client base is overwhelmingly composed of informal sector owner-managed microenterprises. In spite of their obvious potential in poor communities, forms of cooperative enterprise are generally not given much, if any, encouragement. In many developing and transition countries, there is significant ideological/political resistance within the international development community (and not only here) towards providing significant support for – still less, prioritizing – genuine community-based, collective and cooperative enterprise ventures.

In the IC model, however, preferential support for cooperative enterprises was an absolutely core factor in the model and thenceforth in the ultimate success of the regional economy. Support was provided to the cooperative enterprise format on the basis that it was the only enterprise structure that could reconcile the multiple economic, social, political and cultural development goals enunciated by the regional government in Emilia-Romagna, and by the local parish priest and his core team of supporters in the Basque country. Genuine cooperatives not only tend to materially reward their worker-members in excess of the rewards in comparative work in an investor-driven enterprise (wage plus profit share, social benefits, health cover and so on), but the individual psychic benefits derived from greater participation, dignity and control are hugely important in establishing a culture of democracy, equity and cooperation outside of the cooperative. Among other things, this package of benefits more than justified any government financial and other support channelled in the direction of the cooperative sector.

The individual psychic benefits from greater participation, dignity and control are also important outside the cooperative

It is important to note also that, while some of the preconditions for the success of the cooperative sector in both regions were possibly geographically, historically and culturally specific, most of the key necessary preconditions in both regions had to be deliberately created. The mobilizing role of the regional government in Emilia-Romagna and that of the CLP in the Basque region are excellent examples of regional/local 'developmental state' intervention, community development planning and 'social entrepreneurship'. But there is nothing so technically complex in the establishment and operation of the variety of institutional vehicles deployed in both regions that prohibits their replication elsewhere.

At the same time, the use of long-term, 'patient' funds to support longer-term focused cooperatives and, in Emilia-Romagna, other enterprise structures as well, was an initial policy choice based largely on an appreciation of the fact that sustainable development would simply not be achieved any other way. The institutions used to mobilize savings and patiently invest locally were built upon both existing and completely new local financial institutions. With care, motivation, appropriate 'checks and balances' and a willingness to learn from others, there is therefore no real reason why this important feature, too, cannot be established elsewhere (for example, as the Chinese have done since 1980 in their monumentally successful rural industrialization drive underpinned by rafts of newly established rural and urban credit cooperatives).

And finally, the social objectives aspect incorporated into the IC models in both regions requires elsewhere only a willingness to allow development to be seen in the same light. In fact, there are very many examples today where communities in both developing and transition countries have successfully mobilized in order to demand and construct similar institutional structures as found in the Basque region and Emilia-Romagna. But, pointedly, such heretical ideas have generally been actively discredited and blocked by the international donor community, mainly in order to foreclose on any possible 'bottom up' challenges to the neoliberal development framework that they have painstakingly imposed as 'best practice' in most countries across the world. If such artificial barriers were removed, it is very likely that there would be very much more experimentation with the IC model in both developing and transition economies.

Attempts to construct similar institutional structures have generally been discredited by the international donor community

Overall, therefore, the key economic and social preconditions required to repeat at least some aspects of the Basque region and Emilia-Romagna success are not only present in very many developing and transition countries, but it is also very possible to actively establish such preconditions if there is a mind to do so.

Assuming a responsibility towards the local community. In the commercial microfinance model, individual microfinance institutions have little concern with coordinating their operations in order to best support the local community. For example, if any 'funds gap' remains, it is not their concern to deal with it, unless they can see a way – which is not always possible – to make a profit out of so doing.

In both IC models, however, a complex interplay between financial institutions was critical to ensuring that the best development opportunities were simply not overlooked thanks to any funding gaps. In the Basque region, the CLP was the crucial initial catalyst for sustainable development, judiciously reinvesting local savings back into industrial cooperatives utilizing modern technologies, incorporating high skills and producing relatively high value-added products. However, the CLP's rapid growth and financial resources eventually meant it had no option (practically and legally) but to move over to focus on lending to larger business ventures, both cooperative and non-cooperative. But this scaling-up process did not happen (was not permitted, in fact) until the impending vacuum for new start and smaller-scale cooperative ventures was deliberately filled by other local financial institutions, such as Oinari, local government economic development departments, and the regional and local cooperative federations.

In both IC models, a variety of financial institutions ensured that the best development opportunities were not overlooked

In Emilia-Romagna, the local and regional governments and central state funding provided the capital to kick-start the microenterprise, cooperative and SME sectors after 1945. The cooperative banks provided particular impetus for cooperative development, quickly joined by a range of financial programmes specially devised and coordinated by the cooperative movement itself (albeit often financed by regional and local government). Fincooper then took up the challenge to provide accelerated and deeper financial support for the cooperative sector in the late 1960s, particularly with regard to the demand for modern technologies. Finally, in the mid-1990s, further support for cooperatives was forthcoming in the shape of the Coopfond initiative, particularly to convert into cooperatives some of the increasing number of failing investor-driven companies in recession-hit Italy.

Quality, long-term and free-of-charge business development services were critical to supporting the best enterprises. In the commercial microfinance model, little effort is made to offer quality business development services (BDS) in order to ensure the longer-run success of their microloan clients. Experience in both developing and transition countries shows that most microenterprises, especially new starts and early stage ventures, either cannot or will not pay the costs of any BDS provision (and most, in truth, do not need it). Most microfinance institutions thus stick to offering the microloan product on its own, or possibly alongside a very basic BDS provision.

BDS provision to new ventures was an integral part of the loan package

In both IC models, however, in order to ensure the best possible chances of longer-run enterprise survival, BDS provision to new ventures was an absolutely integral part of the loan package. In the Basque region, the CLP developed its own sophisticated in-house BDS provision by establishing the División Entrepresarial (Entrepreneurial Division), a team of specialists able to assess and patiently support new ventures into successful operation. In more than 30 years of operation, only a handful of new cooperative projects failed. When, in the 1990s, the CLP moved to directly support only the very largest ventures, including non-cooperatives, the BDS function within the CLP also changed. BDS was still available for large-ish new starts and the largest existing cooperatives, but responsibility for new starts and smaller cooperatives was passed over to a range of other local institutions, including the cooperative sector's Elkar-Lan cooperative development organization. Elkar-Lan now provides sophisticated, free-of-charge BDS to all new small cooperative development projects in the region showing a demonstrable potential to succeed.

In more than 30 years of operation, only a handful of new cooperative projects failed

In Emilia-Romagna, a very sophisticated regional and local government-coordinated and government-financed BDS structure emerged from the 1950s onwards. Initially, local and regional government economic departments were able to work easily and transparently with the local small business community. In the early 1970s, BDS provision was reformed and strengthened with the establishment of the new regional government's servizi reali. At the same time, as membership increased and with it subscription funds, the cooperative movement developed its own sophisticated forms of BDS to support its existing and future cooperative members.

Conclusion

The IC model pioneered in the Basque region and in Emilia-Romagna is a local financial systems model manifestly associated with the targeting and achievement of sustainable economic and social development outcomes, and thus also sustainable poverty reduction. As noted above, two crucial factors were largely responsible for these positive outcomes. First, the sustainable development-driven 'local savings and investment cycle' within the IC model was quite pivotal to the gradual widening and deepening of the local enterprise and economic base. Second, the deliberate emphasis on supporting various forms of cooperative resulted in a core of quality employment opportunities emerging in a mutually reinforcing local environment marked out by very high levels of equity, dignity, respect, participation, social justice and (thus) probably the highest levels of social capital anywhere in Western Europe.

Both of these crucial sustainable development factors have very little traction in the commercial microfinance model. The commercial microfinance institution is principally concerned with its own survival, not with identifying and supporting the structure of local enterprises associated with the sustainable development and growth of the local economy within which it operates. Put crudely, so long as clients repay their microloan no further concern is generally registered as to the longer-run results and wider opportunity costs. The growing number of microfinance 'cathedrals in the desert' is testament to the fact that very healthy commercial survival is perfectly possible in a locality where the most promising sustainable local economic development and generalized poverty reduction trajectories have been all but abandoned or destroyed. It thus seems clear that the IC model needs to be revisited and the core relevant lessons outlined above factored into the constantly evolving design of local financial systems in both developing and transition economies alike.

Very healthy MFI survival is possible in a locality where the most promising local economic development possibilities have been abandoned

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