# **EUROPEAN INVESTMENT FUND**

**SB/16/16** 7 September 2016

**Document 20-2016** 

# EUROPEAN FUND FOR STRATEGIC INVESTMENTS STEERING BOARD

# **EIF - SME Window EaSI Guarantee Enhancement**

Adopted by Written Procedure with expiry date 21/07/2016

Joint proposal by EC, EIB and EIF



# EIF - SME Window EaSI Guarantee Enhancement

Each transaction under the SME Window of the EU Guarantee implemented by the European Investment Fund ("EIF") is subject to EIF's governing bodies' approval. However, SME Window products also have to be approved by the EFSI Steering Board, jointly with the Managing Director, after consultation with the EFSI Investment Committee (as these terms are defined in the EFSI Regulation).

The purpose of this note is to describe an additional product to be considered under the SME Window, namely the "EaSI Guarantee Enhancement", and to seek its approval by the EFSI Steering Board, jointly with the EFSI Managing Director, by written procedure expiring the 21<sup>st</sup> July 2016. In the meantime, the EFSI secretariat will inform the Steering Board of the outcome of the consultation with the EFSI Investment Committee, following its meeting to be held on 14<sup>th</sup> July 2016.

#### 1. Background

Following the adoption of the regulation (EU) 2015/1017 by the European Parliament and by the Council on 25 June 2015 (the "EFSI Regulation"), the European Union ("EU") and the European Investment Bank ("EIB") signed on 22 July 2015 a guarantee agreement regulating the implementation of the European Fund for Strategic Investment ("EFSI"), as part of the Investment Plan for Europe ("IPE") (the "EFSI Agreement"). In addition, a back to back agreement was signed between EIB and EIF on 22 July 2015 (the "EIB/EIF SMEW Agreement"). The EIB contribution to EFSI amounts to EUR 5bn, which, combined with the EU Guarantee (as this term is defined in the EFSI Agreement) of EUR 16bn, should result in a total investment volume in strategic projects of at least EUR 315bn due to EFSI's objective to mobilise private and public investment. Within this framework, the EIF is engaged in improving access to risk finance for SMEs and small mid-caps by managing the SME Window, while EIB focuses on operations under the Infrastructure and Innovation Window.

At a size of EUR 5bn, the SME Window aims at supporting an investment volume of at least EUR 75bn for the benefit of SMEs and small mid-caps and its deployment entails two key phases:

- Phase I, approved and launched in 2015, composed of:
  - EUR 2.5bn provided by EIB under its own risk to increase the existing equity Risk Capital Resources mandate;
  - up to EUR 1.25bn provided by the EIB under EFSI and backed by the EU Guarantee to allow the frontloading of COSME LGF 2016-2020 budget and InnovFin SMEG 2016-2020 budget (by deploying EUR 1.25n of the EU guarantee which is being gradually released from 2016 onwards once the EU budget commitments under these two programmes become available);
- Phase 2, composed of the EFSI SMEW Equity Product, for a total amount of EUR 1.27bn, the EaSI Guarantee Enhancement (up to EUR 50m) and further products yet to be submitted for approval.

Following the approval of the SME Window frontloading products by the EFSI Managing Director and the EFSI Steering Board in January 2016<sup>1</sup>, and after consultation of the EFSI Investment Committee, authorizing the frontloading of the COSME LGF and the InnovFin SMEG 2016-2020 budget, approval is further sought for the EaSI guarantee financial instrument enhancement ("EaSI Guarantee Enhancement") to add the EaSI Guarantee Enhancement as a new guarantee product benefitting from the EU Guarantee and to frontload the EaSI Guarantee Enhancement 2017-2020 budget on terms summarized below.

Following relevant approvals, the EFSI Agreement will be amended to include the EaSI Guarantee Enhancement.

# 2. Leveraging EaSI guarantee under the SME Window of EFSI

### 2.1 EaSI guarantee financial instrument

EaSI is the programme for Employment and Social Innovation ("EaSI") launched by DG EMPL in 2014 and aiming at contributing to the implementation of the Europe 2020 strategy by supporting the EU's core policy objective of high level employment, guaranteeing adequate social protection, fighting against social exclusion and poverty and improving working conditions. EIF has been entrusted by the EU for the implementation of the first financial instrument launched under the programme: the EaSI guarantee financial instrument (the "EaSI Guarantee"), which covers the microfinance and the social entrepreneurship sectors.

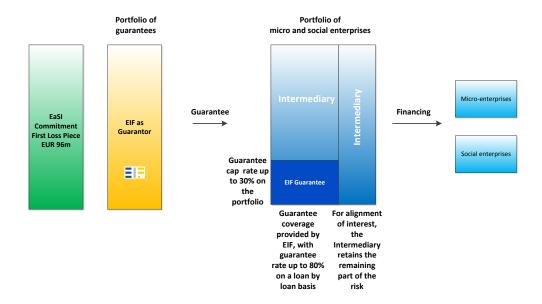
The signature of the delegation agreement between the EU and the EIF took place on 22 June 2015, with the EaSI Guarantee made available to intermediaries via an open call for expression of interest published on EIF's website on 24 June 2015.

The EaSI Guarantee is provided in the form of a first-loss capped guarantee that EIF offers through selected financial intermediaries to cover loan portfolios in the areas of microfinance (targeting micro-borrowers and micro-enterprises) and social entrepreneurship (targeting social enterprises).

The risk-sharing mechanism between financial intermediaries and EIF enables microcredit providers or social enterprise investors, to increase loan volumes and acquire new customers by reaching out to (potential) entrepreneurs/micro-enterprises that they would not have been able to finance otherwise due to risk considerations.

In particular, the **Social Entrepreneurship** initiative under EaSI targets a new sector for EIF, and aims at supporting the achievement of positive social impacts and generating social return.





The detailed terms of the EaSI Guarantee are available on the EIF's website:

http://www.eif.org/what we do/microfinance/easi/index.htm?lang=-en.

# 2.2 Frontloading of EaSI Guarantee under the SME Window of EFSI

The current high demand by financial institutions under the EaSI Guarantee combined with the fact that funds made available by the EU budget for the purposes of providing EaSI Guarantees are allocated through annual instalments, is likely to lead to a pattern where EIF would have to interrupt origination pending each year's allocation being obtained.

Through the EU Guarantee coverage provided by EFSI, a frontloading of the 2017-2020 investment capacity under EaSI could be achieved, which would ensure a more rapid roll out especially over the years 2016-2018.

As of 20 June 2016, EIF has indicatively received 51 applications in 24 countries which should consume and exceed the EU budget made available for the years 2015 and 2016. Under current circumstances, processing of applications received would be delayed in case of full utilisation of the EU annual budgetary commitment.

The indicative budget available under the EaSI Guarantee for the period 2015-2020 amounts to EUR 96m, which is made available on a yearly basis following the decision of the EU budgetary authority. To date EUR 68.8m of this budget have already been committed by the EU to EIF. Depending on an increase of the future budget, beyond the EUR 96m initially earmarked by the EU, the 2017-2020 budget frontloading for this specific product could reach up to EUR 50m.

EaSI Guarantee Enhancement represents the third product of its kind under the EFSI SME Window, following the -similar- implementation of the COSME LGF Enhancement (2016-2020 budget frontloading EUR 500m) and of the InnovFin SMEG Enhancement (2016-2020 budget frontloading EUR 750m).

#### 2.3 Additionality

According to Article 5 of the EFSI Regulation, "EFSI should ensure additionality by helping to address market failures or sub-optimal investment situations and supporting operations which could not have been carried out in the same period during which the EU Guarantee can be used,

or not to the same extent, by the EIB, the EIF or under existing Union financial instruments without EFSI support".

Under the EaSI Guarantee Enhancement, additionality is provided under both pillars:

- (i) the frontloading of 2017-2020 investment capacity under EaSI Guarantee would enable an accelerated implementation (especially over the years 2016-2018) of the product and would allow overcoming the limitation induced by yearly budgetary allocations being lower than demand. Such frontloading, ensuring speeding-up of financing made available to the EaSI Guarantee, would not have been possible without the EFSI support;
- (ii) the investment and guarantee scope provided for under the EaSI Guarantee falls within EIF's core policy to support EU-28 micro and social enterprises. In particular, EaSI targets among its ultimate beneficiaries potential borrowers such as (a) micro-borrowers living in difficult situations wishing to start their own enterprise, (b) micro and social enterprise that could either employ disadvantaged people or provide good or services to underserved community. An accelerated implementation of the EaSI Guarantee, through the frontloading mechanism, could therefore address market failures by enhancing access to finance to population having difficulties in accessing the traditional credit markets.

#### 3. Drawing(s) under EU Guarantee and EIB back-to-back guarantee

The EFSI Agreement will be amended to include the EaSI Guarantee Enhancement as a SMEW Product benefitting from coverage under the EU Guarantee.

Through the back-to-back guarantee provided by the EIB to the EIF under the EIB/EIF SMEW Agreement, EIF will to benefit from a guarantee for amounts that exceed the available EU contribution committed. EIB will in turn obtain coverage under the EU Guarantee. The EU Guarantee covering such frontloading may be either substituted by the subsequent yearly EU contribution committed made available to EIF under the EaSI Guarantee or maintained as additional contribution made available for the purpose of the EaSI Guarantee deployment. It is also expected that the subsequent annual EU contribution committed would reimburse any drawing under the EU Guarantee.

# 4. Legal Structure

EFSI (including its implementation) is regulated by:

- i. the EFSI Regulation, which defines the conditions under which the EU budget is made available to support the EFSI investments through the EIB Group and determines the terms of the EU Guarantee (and therefore the terms under which EIB will make financing/risk cover available to EIF for the EFSI SMEW);
- ii. the EFSI Agreement, that describes the detailed mechanisms of the operation of EFSI and the EU Guarantee; and
- iii. The EIB Guarantee, detailing the terms under which EIF delivers EFSI actions for the SME Window and benefit from the coverage of the EU Guarantee for the SME Window.

The SME Window under EFSI is regulated by the Schedule VII annexed to the EFSI Agreement. Provisions related to the EaSI Guarantee Enhancement have been inserted accordingly.

The SME Window implemented through EIF is governed by EIF's governing bodies for each transaction approval. However, EU Guarantee coverage for SMEW products is subject to the approval by the EFSI Steering Board, jointly with the Managing Director, after consultation with the EFSI Investment Committee.

# 5. Key deliverables

The overall volume of investments triggered by such frontloading will potentially mobilize investments for an amount in the range of EUR 700-800m<sup>2</sup>.

As of 20 June 2016, EIF has signed 25 EaSI guarantee agreements for an amount of EUR 43.4m.

The pipeline remains strong, with 51 formal applications in 24 countries received as of 20 June 2016, and a full utilization of the EaSI Guarantee Enhancement capacity is expected before end 2017.

#### 6. EaSI Guarantee Enhancement features

No changes are foreseen to the terms approved under the EaSI Guarantee, with the exceptions of: (i) geographical focus, (ii) time horizon, (iii) visibility requirements.

As regards the **geographical focus**, EFSI's geographical outreach is EU-28 Member States only. However, the following countries are also eligible under EaSI: Turkey, Iceland, FYROM, Montenegro, Serbia, and Albania. The existing EaSI Guarantee geographical focus should therefore remain unchanged and only transactions with intermediaries in EU-28 will be reported under EFSI.

As regards the **time horizon**, EIF may enter into EaSI Guarantee agreement with financial intermediaries until 30 June 2024, provided that approval from EIF's governing bodies is granted before 1 January 2024. EIF will be in a position to enter into EaSI Guarantee Enhancement agreements until 4 July 2019, however only the commitments signed by 5 July 2018 will count towards the EUR 75bn (based on a EUR 5bn SMEW) that EIF is intended to mobilize under the SME Window. Operations signed between 5 July 2019 and 30 June 2024 shall remain within the remit of the EaSI Mandate and shall not be counted as EaSI Guarantee Enhancement/EFSI operations.

Lastly, operations labelled as EaSI Guarantee Enhancement will have to comply with visibility requirements of EaSI and EFSI and financial intermediaries will be requested to mention the combined EaSI and EFSI support in the contractual documentation with beneficiaries.

\_

<sup>&</sup>lt;sup>2</sup> In line with the EFSI EIF Multiplier methodology