How does a guarantee scheme work?

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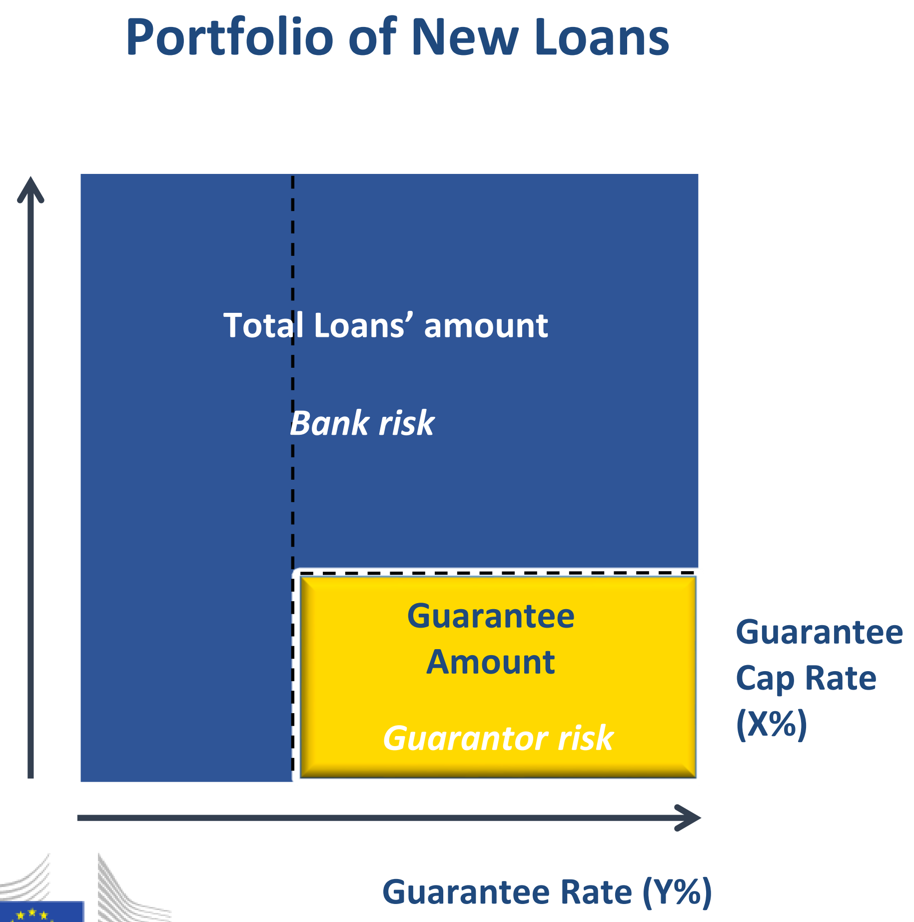
Capped Portfolio Guarantee

Objective: provide **better access to finance to targeted Final Recipients** (typically addressing a market failure identified in ex ante assessment)

- ✓ Providing better access to finance to targeted SMEs (full advantage passed on to SMEs), addressing concrete and well identified market gaps.
- ✓ Leveraging the ESIFs to support financing for SMEs.

The Capped Portfolio Guarantee provides credit risk coverage to intermediaries on a loan by loan basis, **up to a Guarantee Rate**, for the creation of a portfolio of new loans to SMEs **up to a Guarantee Cap Rate**.

First Loss Portfolio Guarantee – *at a glance*



Objective: access to finance, with improved lending conditions for Final Recipients (reduced interest rates and/or collateral requirements)

- **Cap Amount available to cover losses in the Final Recipients loan portfolio;**
- **For each loan defaulting, [Y]% (guarantee rate) of the covered loss is paid to the bank;**
- **This holds until [X]% (cap rate) of the portfolio is covered.**

Capped Portfolio Guarantee

New portfolio of loans

Guarantee Rate:
up to 80%

ESIF contribution

Multiplier*:
(1/Guarantee Rate) x (1/Cap Rate)

Minimum:
(1/0.8) x (1/0.25) = 1.25 x 4 = 5

Cap Rate: determined in ex ante risk assessment (≠ ex ante!) up to 25%

**determined in ex ante risk assessment*

Capped Portfolio Guarantee

Further key features:

- Lending methodology to ensure that the full **financial advantage** is **passed on to SMEs** – reduction of interest and/or of collateral of each and every loan;
- Portfolio must include new loans (no refinancing!), up to EUR 1.5m each (granularity), for a term of 1 to 10 years (Lending policy – CIR 964/2014);
- Loans for:
    - investments in <u>tangible/intangible assets</u>, including for take over of other enterprises if transfer is between independent investors. But <u>no pure financial activities</u>, <u>real estate</u> development or <u>consumer finance</u> can be supported;
    - working capital related to development or expansion ancillary to investments.

Capped Portfolio Guarantee

Further key features (ctd):

- Eligibility criteria to be aimed at (i) reaching a **large number of recipients**, and (ii) achieving sufficient **portfolio diversification** ➔ no overspecialisation!
- No revolving credit lines, no equity, no subordinated or mezzanine debt;
- No fees payable by financial intermediary.
- Alignment of interest:
    - Performance fees;
    - FI to always keep at least 20% of risk in its own books.

Capped Portfolio Guarantee

The set-up of the instrument is State aid cleared:

- At FoF and FI level, State aid free as long as:
  - Remuneration in line with Regulations and market – FInt. selected in open call;
  - FInt. covers the remaining 20% of risk with own resources;
  - Financial advantage fully passed on to SMEs.

- At SME level, under *de minimis* as long as:
  - GGE is below EUR 200k (including cumulations);
  - Other general rules regarding *de minimis.*

Pricing policies flow

Pricing/Collateral Policies

Funding Agreement

MA/FM

Transparent methodology for pricing and collateral requirement

Portfolio guarantee contract

FM/Bank

Obligation to respect the methodology for all the loan included in the portfolio

Loan contract

Bank/SME

Collateral/Interest rate reduction

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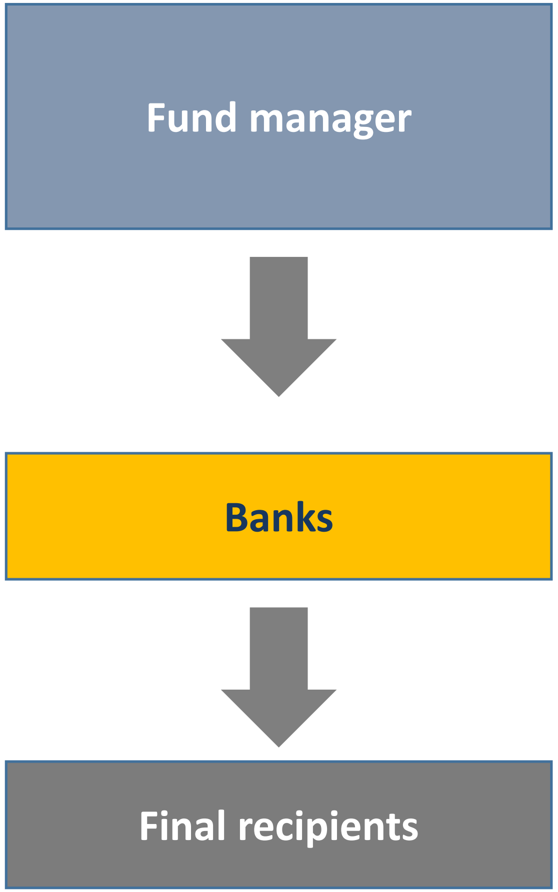
Guarantee - Transfer of benefit to SMEs

FLPG

- Subsidised guarantee
- Delegation principle: eligibility & risk assessment by banks
- Possible capital relief –reduced regulatory capital charge

- Significantly lower collateral requirement
- Reduction of risk related margin (decrease in the interest rate)
- Decreases in fees (based on call application)



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Main advantages of Guarantee instruments

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For MA:

- Leverage effect (> than for a loan),
- Alignment of interest (FInt. “skin in the game”),
- Finance viable investment.

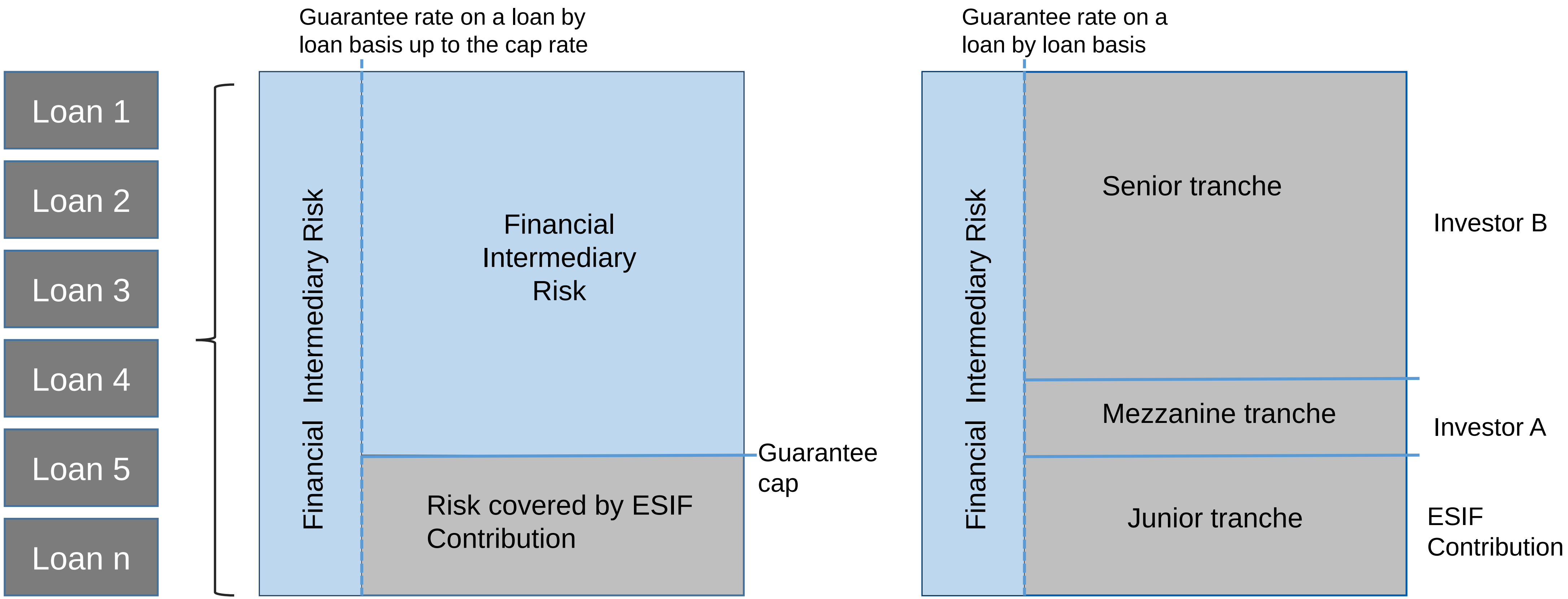
For Banks:

- FInt. risk coverage means reduce the overall exposure of banks (see e.g. following slide),
- Improves bank reputation (more willing to extend loans to SMEs),
- <u>Sometimes</u> allow banks to get capital relief.

For SMEs:

- Easier access to finance, since FInt. risk coverage,
- Collateral reduction,
- Interest rate reduction (cost of risk should be reduced) (< than for a loan).

Capped vs Uncapped Guarantee



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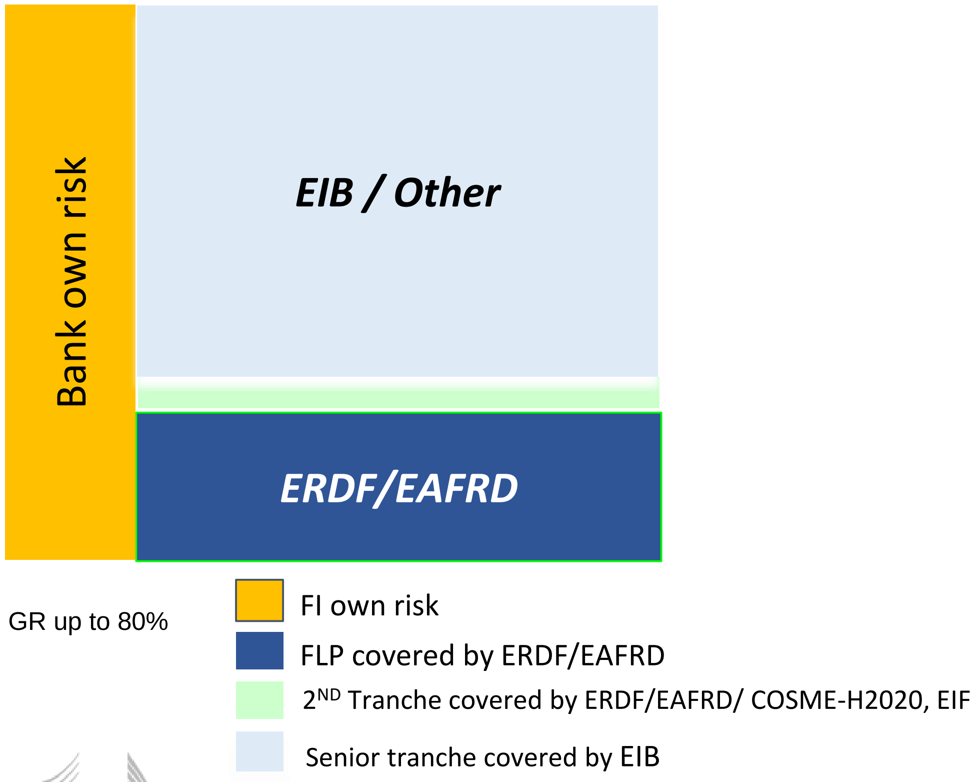
SME Initiative
General overview

- Legal basis of the SME Initiative: Article 39 CPR
- Key objectives
  - Leverage EU budget by mobilising private resources
  - Incentivise financial intermediaries to extend new debt instruments (loans, leases, guarantees) to SMEs
  - Enhance access to SME finance through a reduction of the overall interest rate charged (transfer of financial benefit)
  - Provide loan loss protection and capital relief on the portfolio to be originated

- Two risk-sharing instruments endorsed by the European Council:
  - **Option 1: Uncapped portfolio guarantee facility** for portfolios of new SME loans/leases up to 80% guarantee rate
    - *Signed mandates in Spain, Malta, Bulgaria, Finland and Romania*
  - **Option 2: Securitisation** instrument for portfolios of both new and existing SME loans, where the originators undertake to provide new financing
    - *Signed in Italy*

Option n°1
Uncapped Guarantee instrument

New Portfolio of debt finance



Option n°1:

Provides uncapped portfolio guarantees and envisaged partial capital relief to banks building up new portfolios of loans

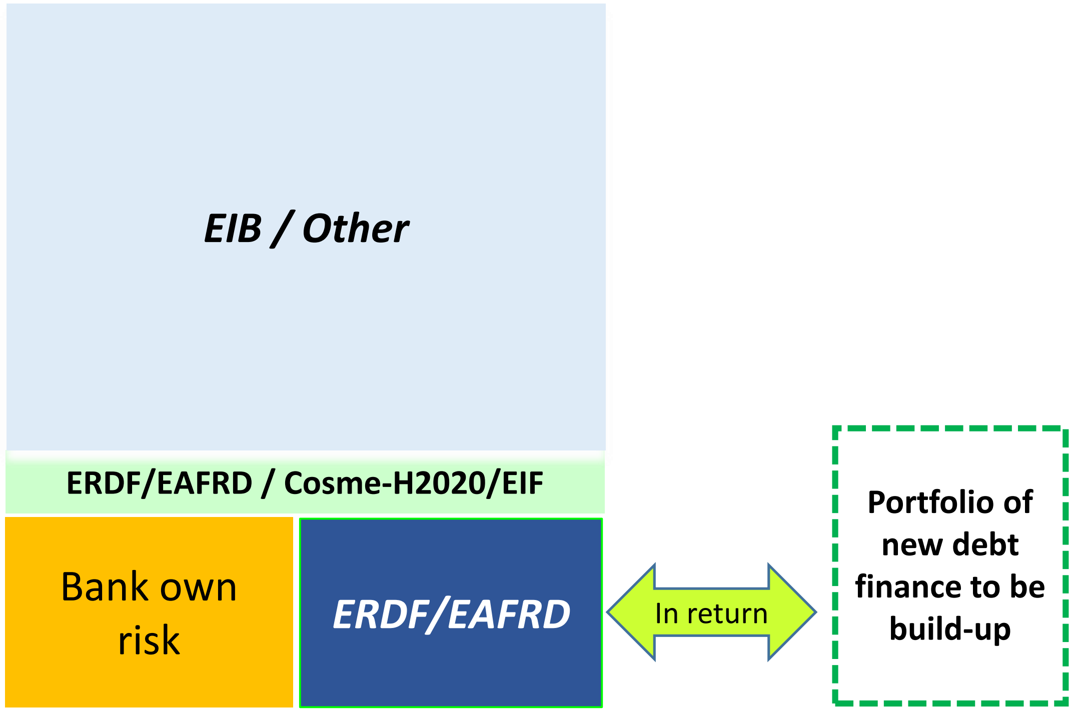
Description:

- Originators (*gradually*) builds-up a portfolio of new SME loans;
- EIF issues uncapped portfolio guarantees (up to 80%) and shares the risk with banks;
- ERDF/EAFRD are used to cover the first-loss piece;
- EU funds from COSME/HORIZON 2020 and the EIF join to absorb, along with ERDF/EAFRD, the second-loss piece;
- EIB and possibly NPB guarantee the senior tranche.

In return the originators will have **to transfer benefits of the instrument to the SMEs** in the form of acceptance of higher risk clients, reduction of collateral requirements and/or reduced pricing

Option n°2 *Securitisation*

Existing portfolio (on the book of the Bank) → Creation of a New Portfolio



Option n°2:

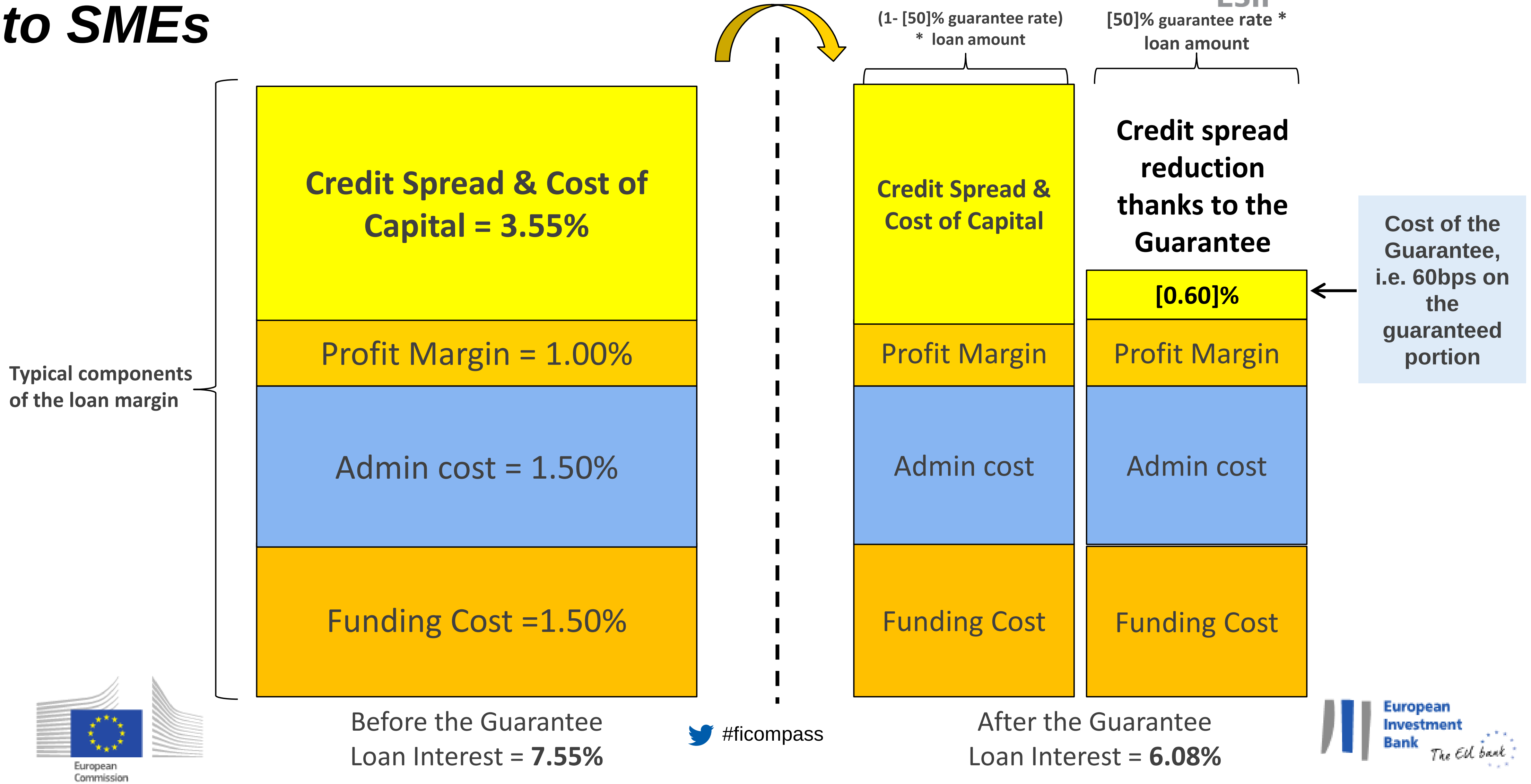
Securitisation instrument can be backed by portfolio of existing SME loans

Description :

- A portfolio of existing SME loans is identified
- 50% of the first-loss piece is retained by the originator and 50% is covered by ERDF/EAFRD
- The risk of the second-loss piece is covered by ERDF/EAFRD, EU funds from COSME/HORIZON 2020 and the EIF. Originator possibly retains 5% of the risk
- EIB and third-party investors purchase or guarantee the senior tranche up to agreed maximum amounts

In return the originators explicitly undertake to **provide new financing** (*amounting to multiple of the EU Funds contribution*) **to SMEs** in the relevant regions in line with the eligibility criteria the EU funds contributed in the structure

SME Initiative
Option 1: Transfer of Benefit to SMEs



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All numbers are indicative and for illustrative purpose

SME Initiative
Main Benefits

For SMEs	Easier/better access to bank financing	Significant Transfer of F. Advantage: ESIF have a zero cost on the equity tranche	More opportunities for innovative SMEs and new technology-based firms	Helps to mitigate financial market fragmentation in the EU in terms of credit cost
For Member States / Region	No national co-financing required State Aid is cleared, no additional negotiation of state aid schemes required	Ex ante assessment already done by the EC Clear governance structure	Aligned to MS priority objectives SME credit growth may drive economic growth	More efficient use of ESIF Transition from a subsidy culture to revolving financial instruments
For Financial Intermediaries	Credit protection	Capital relief	Access to new clients/segments	High visibility for SME support

SME Initiative:
Deployment (1)

SME Initiative Finland:

- Signature of the relevant agreements between the Republic of Finland, the European Commission, EIF and EIB: **14/09/2016**
- Expected **EUR 400 million** of new SME financing to be provided
- Call for expression of Interest published: **15/09/2016 with deadline for application 31/03/2017**
- 6 financial intermediaries applied for a total portfolio of EUR 690m
- 3 financial intermediaries are now providing loans, others to join in the near future
- Very good market response, “oversubscribed” by EUR 290m
- More than **EUR 80 million** already committed to more than **130 SMEs** according preliminary data.

SME Initiative Romania:

- Signature of the mandate agreements between the Republic of Bulgaria, the European Commission, EIF and EIB: **20/10/2016**
- Expected **EUR 540 million** of new SME financing to be provided
- Call for expression of Interest published: **21/10/2016** with deadline for application **31/03/2017**
- 5 transactions signed up for SMEi Romania, namely Banca Comerciala Romana, Banca Transilvania, Bancpost SA, Procredit Bank Romania, Raiffeisen Bank Romania, ProCredit Romania, Libra Bank, ING for the amount of EUR 540m.
- Number of SMEs loans signed: **25** for the amount of **EUR 12m** as of **Q2 2017**

SME Initiative:
Deployment (2)

SME Initiative Bulgaria:

- Signature of the mandate agreements between the Government of Bulgaria, the European Commission, EIF and EIB: **02/03/2016**
- Expected **EUR 600 million** of new SME loans to be provided
- Call for expression of Interest published: **17/05/2016** with deadline for application **30/11/2017**
- 10 transactions signed with Financial Intermediaries for the amount of EUR 608m
- Number of SMEs loans signed: **1,471** for the amount of **EUR 150m** as of Q2 2017