AECM's comments on the interim evaluation of the programme for the competitiveness of enterprises and small and medium-sized enterprises (COSME) (2014-2020)

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INTRODUCTION:

The European Association of Guarantee Institutions, AECM, warmly thanks the European Commission for the possibility to provide feedback on the interim evaluation of the programme for the competitiveness of enterprises and small and medium-sized enterprises (COSME) (2014-2020) focussing on the activities of the period of 2014 to 2016.

Many of AECM's 42 members have long-lasting experiences in implementing the EU guarantee instruments. To illustrate: The first guarantee contract ever signed by the European Investment Fund (EIF), to whom the EU Financial Instruments are entrusted, was with one of AECM's Austrian members in December 1998. Today, 16 of AECM's members are using the Loan Guarantee Facility for Growth (LGF) of the COSME programme, thereby facilitating two thirds of the investments made possible thanks to the LGF[1]. The same applied also to the guarantee instruments of the predecessor programmes CIP and MAP having made guarantee institutions the natural partners and allies of the EU institutions and the EIF for implementing the EU guarantee instruments.

Therefore, the design of EU guarantee instruments and as to COSME of the LGF is of utmost importance for AECM and its members. Based on the long-lasting practical experience gained by AECM's members in using financial instruments and due to the important role they have as financial intermediaries for the LGF, AECM would like to submit the following comments and requests as contribution to the interim evaluation of COSME.

GENERAL COMMENTS

AECM strongly supports COSME's specific objective "to improve access to finance for SMEs in the form of equity and debt" as well as the operational objective to "provide enhanced access to finance for SMEs in their start-up, growth and transfer phases through a debt financial instrument and an equity financial instrument". These objectives possess a continued relevance contributing also to the Union priorities of smart, sustainable and inclusive growth.

Regarding the EIF, we rate its role in the implementation process of the financial instruments with guarantee institutions very positively. The members of AECM using the EU guarantee instruments enjoy a long-lasting excellent, effective and smooth cooperation with the EIF and report that the EIF has always been very supportive in explaining the process and conditions to be met to sign an agreement.

As to the design of the LGF, in general it addresses our members' needs enabling them to support even more micro, small and medium-sized enterprises (MSME). Right from the start it needs to be stressed that the LGF has proven to be very successful and without any doubt there is a continued need for it. Yet some features of the LGF could be improved to make it even easier to use and to broaden its scope of application and effectiveness supporting actually more MSME.

[1] Per mid-June 2017 the EIF committed EUR 475m out of EUR 771m, i.e. to 62% of the budget to guarantee institutions. The EIF cautiously estimates that the financing volume facilitated by guarantee institutions amounts to EUR 18.7 bn out of EUR 24.7 bn, i.e. to 76%.

THRESHOLD OF 150,000 EUR

One of the most pertinent issues where we see an urgent need to modify concerns the current requirement for differentiation between loans up to 150.000,00 EUR and above and if above the examination if the SME meets the criteria to be eligible under the COSME programme and does not meet the criteria to be eligible under the SME window in the Debt Facility of the Horizon 2020 programme.

From AECM's point of view, this threshold, which got newly introduced in the current programme period, should ideally be entirely abolished allowing all kinds of high-risk financing under COSME without any examination whether it is an innovative project to be financed or not. This would make the application of the LGF simpler and more practical, terminating an excessive administrative burden for present financial intermediary and, at the same time, would attract more financial intermediaries. The important consequence would be that accordingly more MSME could be supported and their financial needs which are also often higher than 150.000,00 EUR could be better met.

AECM and its members are fully aware that any modification on that ground would require a revision of the legal basis of the program and therefore an agreement decided upon jointly by the European Parliament and the Council of the European Union. Yet, we are confident that this effort would be worthwhile to get back to the former status quo of CIP and MAP in order to best comply with SMEs' market needs.

Yet, if it were not possible to abolish the threshold of 150.000,00 EUR, the second-best option would consist in a substantial increase to minimum 500.000,00 EUR to correspond better to the needs of MSMEs. Such an increase would extend the scope of the LGF to SMEs not eligible under InnovFin and speed up its delivery on the ground.

BALANCED RELATIONSHIP BETWEEN COUNTER-/CO-GUARANTEES AND DIRECT GUARANTEES

The LGF is provided to guarantee institutions in form of counter-guarantees or co-guarantees and secondly the LGF is provided as direct guarantee to any other financial intermediary, usually to commercial banks. From AECM's point of view there remains room for improving the coherence between these two ways.

In some countries, where no operative guarantee institution exists like, for instance, in Malta or in Cyprus, or where guarantee institutions do not cover all instruments demanded by SMEs, direct guarantees are the only way to reach out to SMEs or to cover the whole variety of instruments. Yet, in an increasing number of countries in which guarantee institutions are established direct guarantee contracts are concluded sometimes even in parallel to counter-/co-guarantee contracts. For the LGF this is the exception but for instance is the case in Estonia (COSME LGF counter-guarantee contract of the EIF with KredEx = a guarantee institution as well as COSME LGF direct guarantee contract of the EIF with Swedbank = a commercial bank) or in Bulgaria (contracting partners of the EIF for the LGF are the National Guarantee Fund as well the CIBANK).

AECM requests that the provision of EU guarantees should be adjusted to the characteristics of the Member States or regions since the involvement of guarantee institutions results in many advantages. To name only a few:

- Compared to direct lending programmes, credit guarantee schemes have much lower initial cash flow needs, and as such, have a high leverage (or multiplier) component which means a more efficient use of public money. Therefore, they can also be used when fiscal constraints are tight and public resources are scarce.
- Involving guarantee institutions in the lending chain results in a higher degree of risk sharing which is advantageous for all parties involved.
- Having a promotional task, AECM's members support only those MSMEs that have a real need. Guarantee institutions fill the market gap as to MSMEs' access to finance also in times of crisis, when they are even more needed, due to their promotional mission.
- Since AECM's members are cooperating with all commercial banking players in their domestic markets, they cover all MSMEs.
- Guarantee institutions are characterized by a deep knowledge of the local market. They recognise soft factors and address financial illiteracy. Due to their proximity to MSMEs who are sometimes indirectly or directly involved in the decision-taking process they are able to thoroughly assess SMEs' needs for financing which enables them to select projects with a higher quality thereby creating a significant economic additionality. They are able to implement tailor-made financial instruments locally, thus adapting to the needs of the markets and having a better market and higher risk focus, hence creating additionality.
- Moreover, they ensure a better visibility of funding solutions.

To conclude, the macroeconomic impact of the LGF provided as counter-guarantee on the economy is significantly higher thanks to a higher input/output relation and a higher economic additionality in terms of innovation, employment and growth. Accordingly, to achieve greater coherence, the conditions for counter-guarantees should be set in a more favourable way. Thus, it would be desirable to build up on the differentiation of the LGF treating counter-guarantees in a more favourable way than direct guarantees when determining which cases imply higher risks. AECM explicitly thanks DG GROW for this distinction and strongly encourages to continue in this direction. One option could be during the selection process of each applicant: As stipulated in the call for expression of interest of the COSME loan guarantee facility, part of this process is an applicant based scoring in which a set of criteria is evaluated. One could include a criterion examining if a well-functioning guarantee institution is already in place in the applicant's country. If the applicant is from such an institution, it would give his application a better quality. In any case, a more profound analysis of a potential crowding-out effect should be undertaken when examining an application.

AECM is convinced that harmonization of the two forms of the LGF can result in beneficial synergies for the whole financial and economic environment. Financial instruments are useful, but crowding out instead of complementarity has to be avoided. We should join all the forces and resources available to maximise the synergies to overcome the near future challenges and AECM and its members are ready to do so.

To avoid overlapping of funding schemes, be it of national with European be it of Europeans with Europeans, a market analysis in form of a thorough ex-ante assessment should be done. Properly and duly undertaken, it reveals which funding possibilities are already in place and determines correctly whether complementary support is still needed, thus substantiating the existence of a gap and potential market failure. By means of such an evaluation negative spillover effects would be avoided.

ADEQUATE FUNDING

AECM underlines that the LGF is indispensable for helping MSMEs in getting access to finance and therefore, needs consistently be strengthened. Given the importance of the LGF for the support of SMEs, we have a profound interest in relying on the EU to endow it with sufficient funding. Accordingly, we were delighted to learn that the initially envisaged funding for COSME has been more than doubled most of all thanks to EFSI 2.0.

The LGF is demand-driven meaning that the allocation of funding takes place based on the demand expressed by financial intermediaries. Even though the budget allocation shows a clear priority setting to support access to finance, there has been an overall increasing emphasis on the LGF: The share of the budget planned for the LGF amounted in 2015 and 2016 at 72% of the total budget planned for this specific objective compared to 63% in 2014.

On the other side, it needs to be taken into account that following the Brexit the UK's net contribution of annually more than 10 bn EUR will be lacking. At the same time, the EU is expected to play a bigger role in new policy areas like migration, internal and external security or defence.

In many countries in Europe loan financing remains the key resource for financing of MSME so that in line with market requirements and in a practice-oriented way the focus should be straight away on guarantee instruments. Therefore, we request the European legislators to continue to make sure that the financial need of SMEs is acknowledged and successfully addressed by ensuring that sufficient financial resources will be made available for the LGF. No funding gap may arise till the successor programme becomes operative.

STATE AID

There is a need to modify and harmonise the state aid regulation in order to make it more practice-oriented and more market conform.

In the first place, the decisive factor should be the entrepreneur whose financing project should be treated the same way no matter in which region or Member State the LGF is provided (e.g. at present, an entrepreneur applying for a loan receiving a guarantee from a German guarantee bank which has signed an agreement for the LGF is treated differently when applying for the same loan for the same project as a bank in Austria receiving a guarantee from the Austrian promotional institution aws which has an agreement with the EIF for the LGF).

Furthermore, state aid regulation should correspond to the market situation. In order to facilitate access to finance for a larger number of MSMEs, the Commission Notice on the application of Articles 87 and 88 of the EC Treaty to State aid in the form of guarantees (2008/C 155/02) should be revised: Instead of having a fixed safe-harbour premium of currently 3.8 %, a more flexible solution should be found to comply well with changing economic environments. Thus, the current level of the minimum fee prescribed in this communication is very high compared with current interest rates for loans which results in a negative impact on SMEs' access to finance.

Finally, focussing again on the entrepreneur, there should be no difference no matter whether the LGF is provided as counter-guarantee or as guarantee. At present, if the LGF is provided as direct guarantee to a commercial bank, there is no state aid involved. If the LGF is provided as counter-guarantee, it depends: if the guarantee institution is private without public support, no state is involved; if the guarantee institution is either private with public support (e.g. in Portugal) or if the guarantee institution is public itself (e.g. in the Baltic countries, in the Czech Republic to mention only a few) it depends on the nature of the guarantee product, for instance in Poland the market-oriented guarantee instrument under COSME does not constitute state aid. Yet, if no market-oriented price is paid for the guarantee, it is state aid and at least the counter-guaranteed part of the guarantee should be excluded from the calculation of the gross grant equivalent of the guarantee so that the entrepreneur would benefit at least partly from the state aid consistency of the LGF.

DURATION

A revised approach of the duration would be welcomed. At present, individual financing transactions must have a minimum duration of 12 months and a maximum duration of 10 years. The minimum duration should be shorter and the maximum duration should be longer, at least 15 years, so that more MSMEs could benefit from the LGF.

Planning certainty is especially important for small companies. Many investments in buildings, for instance in connection with increasing production capacity, are part of a long-term strategy and clearly exceed the ten-year term. In order not to disadvantage small companies via-à-vis larger ones, their access to longer-term finance should be made easier. The basic principle that needs to be applied here is to achieve congruence between use duration and funding duration.

SIZE & SCOPE

In order to give every guarantee institution a chance to sign an agreement with the EIF, it would be preferable if the size of the contract did not matter. This is of course more valid for the InnovFin SME Guarantee Facility than for the LGF.

The LGF should also be applicable to mid-caps. Despite their difficulties in financing their investment, “non-innovative” mid-caps cannot benefit neither from InnovFin nor from COSME as the former is dedicated to innovative businesses and the latter targets SMEs. In order to tackle this financing gap, mid-caps up to 3.000 employees should be made eligible to COSME so that its scope includes the “non-innovative” ones. It would widen the range of COSME beneficiaries and strengthen the continuum of financing for non-innovative businesses.

BUREAUCRACY

As stated above, it would alleviate the administrative burden of the guarantee institutions if the threshold of 150.000,00 EUR were abolished. Yet, there is more room to simplify the regulatory architecture and thus, the implementation.

It seems that the administrative requirements have been increasing slowly but constantly from one programme to the other. One needs to be very careful in striking the right balance between transparency, administrative burden, proportionality and costs. The costs (direct and indirect) generated by the programme should always remain proportionate to the benefits generated.

So far, AECM's members cope well with the requirements even though they start regarding them as being too extensive. To illustrate:

Regarding the visibility requirements it would be easier to do more if a budget were foreseen. Yet, normally additional requirements are entirely up to the financial intermediary in both regards, the actions as such as well as the financing of such additional activities.

An example to reduce existing reporting and other administrative requirements: Especially where the partner banks are responsible for the reporting of the guarantee contract, they seem to encounter reluctance of their SME clients when it comes to reporting back the yearly number of employees of the company.

Consequently, the reporting requirements laid down in the legal basis should be as simple as possible, should not be further tightened, thus preserving the essential principle of proportionality. In general, the formalities and controls should be reduced to the strict necessity. This also includes to reduce the number of audits and to streamline them.

Unintended by the EU but has happened in practice were adaptations of reporting requirements for ongoing agreements; such changes of regulatory requirements should be avoided to not cause unnecessary and costly changes in IT systems.

It should be ensured that the rules for all EU guarantee instruments (from COSME, the structural funds, InnovFin, the cultural and creative sector, etc.) are ideally identical in form of a common rule book or otherwise as much aligned as possible. Greater complementarities, improved possible combinations and more synergies between existing instruments and players at all levels, i.e. regional, national and supranational, would lead to align incentives and create "win-win" situations for all players along the guarantee value chain, including public authorities, guarantee institutions, banks, and MSMEs. As an example serves the combination of grants and financial instruments. DG AGRI's official statement on the combinability of COSME counter-guaranteed financing and grants under local Rural Development Programmes helped considerably more credit constrained SMEs to get financing for their projects that before had been put on hold and sometimes had even failed.

ADDITIONALITY CRITERIA

The LGF provides financing of transactions which otherwise would not get financed either by using the LGF for riskier loans or by using it to substantially increase the volumes. Some members of AECM noted critically that these additionality criteria are too restrictive leaving insufficient flexibility especially to those financial intermediaries that already provide a wide range and a large volume of loans. Thus, we would prefer if the existing criteria could be interpreted more extensively based on a qualitative approach to better fit the market reality.

There is a strong need for guarantees to cover unsecured loans to non-innovative SMEs and small Midcaps, financing intangible investments in key areas for their competitiveness such as robotization, digitization, energy efficiency and internationalization. These investments are also key to support the factory of the future priority. Therefore, a third additionality criterion should be added, considering subordinated loans additional as such in order to provide specific support from the EU targeting those investments which are essential for the development and competitiveness of businesses. At the same time, it would incentivize private banks to enter this risky loan financing segment while benefiting from a guarantee being counter-guaranteed from the LGF.

OUTLOOK TO THE NEXT PROGRAMME GENERATION

The guarantee instrument in form of a counter- or co-guarantee is well recognised at international, European, national and regional level and is still needed, thus deserves entire support. This is also reflected in the fact that the LGF is one of the key actions of the COSME programme.

Experience has shown that the LGF like its predecessors, the SME guarantee facility under CIP and the guarantee instrument under MAP, promotes well MSMEs' access to finance. In order to achieve higher leverage rates and use public money in a better way, it is important to involve the EU level in the risk sharing chain. Accordingly, this instrument has been and continuous to be relevant, effective and has an EU added value in addressing the market failure with which MSMEs are faced in accessing finance.

Also in the future, the demand for such public support in form of an EU counter-guarantee instrument will remain since likewise the market failure will remain. Therefore, AECM strongly encourages the EU institutions to continue, to strengthen and to enlarge the scope of the LGF taking into account the above-mentioned requests for optimising the LGF since its objective of improving access to finance has been achieved and given that the LGF still is pertinent to the needs, problems and issues it was designed to address. For supporting and sustaining economic growth in Europe, it remains essential to strongly promote MSMEs.

Guarantee institutions are the natural partners in implementing the LGF. The existing close integration of intermediary organisations for the delivery of the programme has proven its success and should be continued[2].

Coherence between programmes remains key and more coordination is needed, for instance, between the implementation of central EU financial instruments and instruments established under ESIF. It should be avoided that for example the LGF covers working capital, whereas there are restrictions in this regard to be applied under ESIF.

Time lags between the LGF and the operative start of its successor instrument under the post-2020 Multiannual Financial Framework (MFF) should be avoided. Stability and continuity of this instrument ideally adapted as laid down in this paper are of utmost importance for the smooth implementation via guarantee institutions.

In this context, we would like to stress that we don't see any need to create new actions. The LGF works well and like its predecessor instruments has stood its test. We would appreciate a continuity of this well-proven counter-guarantee instrument. In general, it can be stated that we don't see a need for niche products which are neither needed nor easy to implement.

The LGF constitutes a valuable extension for the activities of guarantee institutions enabling the latter to support even more MSMEs in addressing their specific individuel financing needs and getting access to finance. As follows from the above, the conditions of the LGF should be improved to enable guarantee institutions to reach out to even more SMES including start-ups and scale-ups.

[2] Per end of May 2017, only 6% of the funding targeted directly the stakeholders

For upcoming programme periods, it would be appreciated to have a clearer picture of the possibility to combine different EU financial resources right from the start. In order to reach out to SMEs as easily and as effectively as possible, it is imperative that the blending of different types of EU funding is made possible at the beneficiary level in accordance with a clear statutory regime. Situations in which a Member State interprets, for instance, article 59 paragraph 8 of Regulation (EU) No 1305/2013 titled "Fund contribution" which lays down provisions on co-financing levels within Rural Development Programmes (RDP) in the way that COSME funding for the agricultural sector cannot be combined with resources from the European Agricultural Fund for Rural Development (EAFRD), whereas the Directorate-General for Agriculture and Rural Development states constantly that this is possible at the beneficiary level should be avoided.

As to discussions underway to combine the programmes COSME and Horizon 2020[3] under the post-MFF AECM would like to underline that no matter what the result, it is vital that the conditions for EU guarantee instruments will become simpler (cf. above), processes will be leaner, synergy effects will be created and most of all the share dedicated to MSMEs will constitute an appropriate share.

Finally, and in accordance with the operational objective to "provide enhanced access to quality information to both SMEs and policy makers on SMEs access to finance and growth" we would highly appreciate if the data available in this area would be increased or if access to such already existing data would be made public. It is self-evident that AECM and its member organisations are prepared to help in an improved data collection through their networks.

We cordially ask the European Commission to take our reflections as explained in this position paper into kind consideration for the interim evaluation of the COSME programme.

It goes without saying that AECM is happy to continue contributing to the important discussion about this evaluation and keeps on doing so also for the next evaluation of the LGF which should be done until 2020 as well as for the design of the LGF's successor, i.e. for the preparation of the future programme under the post-2020 MFF always with the aim to achieve the best benefit possible for SMEs fostering their access to finance and thereby their growth in an optimal way.

[3] The EU Framework Programme for Research and Innovation

About AECM and its members:

AECM's 42 members operating in 26 countries in Europe are mutual-, private sector guarantee schemes, public institutions - either guarantee funds, national promotional institutions or national promotional banks - or mixed. They all have in common the mission to support MSMEs during their whole business cycle in getting access to finance, thus, to foster economic growth, innovation, digitization, job creation, and social integration. More precisely, they promote MSMEs by providing guarantees to them as well as to entrepreneurs and freelance professions who have an economically sound project but do not dispose of sufficient bankable collateral. AECM's members in turn receive a counter-guarantee from regional, national and European level.

Guarantees are a viable tool to reduce the risk of lenders and to support businesses that are constrained in their access to finance. Accordingly, credit guarantee programs continue to be the most widely used instrument at governments' disposal to ease SME access to finance, one of the reasons being that guarantee products have positive macroeconomic effects, meaning that the taxpayers' costs due to default payments are outweighed by the positive stimulating effects of guarantees – such as on employment and innovation – for the economy.

At the end of 2016 AECM's members had over 85 billion of guarantee volume in portfolio, thereby granting guarantees to more than 3.1 million MSMEs.

AECM represents the political interests of its members both towards the European Institutions, such as the European Commission, the European Parliament and the Council, as well as towards other, multilateral bodies, among which the European Investment Bank (EIB), the European Investment Fund (EIF), the Bank for International Settlement (BIS), the OECD, the World Bank Group, etc. It deals primarily with issues related to prudential supervision, to state aid regulation relevant for guarantee schemes within the internal market, to SME policy, and to European support programs also for the agricultural sector.