Comments of UEAPME and AECM concerning the design and implementation of EU financial instruments – joint requests for the EU mid-term review

A / Introductory remarks

UEAPME is the employers' organisation representing crafts, trades and small and medium-sized enterprises (SMEs) from the EU and accession countries at European level. UEAPME has 65 member organisations, which represent crafts and SMEs across Europe, covering over 12 million enterprises with 55 million employees.

AECM's 41 members, who are mutual / private sector guarantee schemes, public institutions or mixed, all have in common the mission of supporting SMEs in getting access to finance by providing guarantees to SMEs who have an economically sound project but do not dispose of sufficient bankable collateral. AECM's members, who at the end of 2015 had around 81 Bn EUR of outstanding guarantee volume, in turn receive a counter-guarantee from regional, national and European level.

Many of AECM's members have been using EU Financial Instruments, which are designed by the European Commission and managed by the European Investment Fund (EIF), right from the start in 1998. More than 50% of the SME Guarantee Facility under the EU programmes MAP, CIP and COSME were / are channelled via AECM's members.

B / Comments

Based on this long-lasting experience as financial intermediaries and taking into consideration the target group of the EU financial instruments, i.e. the SMEs, UEAPME and AECM would like to raise the following requests as contribution to the EU mid-term review:

- **Guarantees as an important instrument to foster innovation, growth and employment**

Guarantees are a viable tool to reduce the risk of lenders and favour the provision of financing to viable businesses that are constrained in their access to finance. Thus, thanks to guarantees SMEs get access to finance for economically sound projects at all or at better conditions. Accordingly, credit guarantee programs continue to be "the most widely used instrument at governments' disposal to ease SME access to finance" (OECD, '*Financing SMEs and Entrepreneurs: An OECD Scoreboard 2016*[1]'). They expanded substantially in the years 2007-2011, as governments responded to the financial crisis and are "increasingly targeting young and innovative firms to boost employment and value added" (OECD, '*Financing SMEs and*

[1] OECD Scoreboard 2016: Financing SMEs and Entrepreneurs, OECD Publishing, Paris, Chapter I.7.a 'Government Policy Responses 2014-15', p.71, retrieved from the www via http://www.keepeek.com/Digital-Asset-Management/oecd/industry-and-services/financing-smes-and-entrepreneurs-2016_fin_sme_ent-2016-en#.WlPgVa6nHIU , see also OECD Scoreboard 2015 (under 'previous versions')

Entrepreneurs: An OECD Scoreboard 2016'[2]). One of the reasons is that guarantee products have positive macroeconomic effects, meaning that the costs for the taxpayers due to default payments are outweighed by the positive stimulating effects of guarantees – such as on employment and innovation – for the economy.

Credit Guarantee Institutions imply several other advantages like, for instance, the following:

i. 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.
ii. Guarantee institutions are characterized by a deep knowledge of the local market. By virtue of their proximity to SMEs who are sometimes indirectly or even 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.
iii. Since guarantee institutions work together with all banks in their respective region or country, they are able to cover all SMEs.
iv. Guarantees are less distortive for competition compared to grants or public loans.

- **Thorough ex-ante assessment**

In order to avoid an overlapping of funding schemes be it of national with European be it of Europeans with Europeans, the ex-ante assessment needs to be carried out in a more thoroughly way. Properly and duly done, it reveals which funding possibilities are already in place and determines correctly whether complementary support is still needed.

- **Improving the Input-/Impact-relation of public funds by enforcing counter guarantees (e.g. by more favourable conditions for counter-guarantees)**

The EU guarantee facility is channelled by the EIF either via guarantee institutions in form of a counter-guarantee (= EIF, guarantee institution, commercial bank, customer) or via commercial banks in form of a direct guarantee (= EIF, commercial bank, customer). In some countries, where no guarantee institution exists like, for instance, in Malta, 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

[2] OECD Scoreboard 2016: Financing SMEs and Entrepreneurs, OECD Publishing, Paris, Chapter I.7.b 'Government Policy Responses 2014-15', p.74, retrieved from the www via http://www.keepeek.com/Digital-Asset-Management/oecd/industry-and-services/financing-smes-and-entrepreneurs-2016_fin_sme_ent-2016-en#.WlPgVa6nHIU , see also OECD Scoreboard 2015 (under 'previous versions')

guarantee contracts are concluded sometimes even in parallel to counter-guarantee contracts.

In case of a counter-guarantee,

- the impact on the economy is higher thanks to a higher input/output relation and a higher economic additionality in terms of innovation, employment and growth (KPMG 2016 – "The importance of Financial Intermediaries in SME financing and assessment of different economic effects especially of EU Financial Instruments in light of direct guarantee vs. counterguarantee contracts");
- since guarantee institutions work with all banks in their region / country, they reach out to all SMEs and not only to a specific customer base;
- guarantee institutions provide guarantees on an individual basis, thus bringing in their specific knowledge on the local SME market including the recognition of soft factors and addressing the so-called financial illiteracy;
- guarantee institutions fill the market gap as to SMEs' access to finance also in times of crisis, when they are even more needed, due to their promotional / self-sustainable mission.

In conclusion, the macroeconomic impact of counter-guarantees is significantly higher compared with direct guarantees and accordingly, the conditions for counter-guarantees should be set in a more favourable way. Such favourable conditions could, for instance, consist in better pricing (e.g. InnovFin). In those cases, in which the EU guarantee is for free, (e.g. COSME), a more convenient treatment of counter-guarantees could be achieved in the course of 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.

- **Review of the EU Communication C155/2008**

In order to facilitate access of a larger number of SMEs to guarantee / counter-guarantee schemes, it is necessary to review the communication no. 155/2008 by updating the rating and the level of the guarantee fees in accordance with the new economic environment of the countries after the financial crisis. 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.

- **Sufficient funding for COSME and InnovFin**

Given especially the importance of the COSME guarantee facility for the support of SMEs and also in mind the strong demand for the InnovFin guarantee instrument, we have a profound interest in relying on the EU to endow these instruments 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. Therefore, we request the European legislators to continue to ensure that the financial need of SMEs is acknowledged and successfully addressed by ensuring that sufficient financial resources will be made available.

- **Scope of application to comply with SMEs' needs**

  The eligibility criteria of transactions should be defined in accordance with SMEs' needs. In this respect, we warmly welcome the change of InnovFin covering in future also mezzanine products like subordinated loans, which are used by traditional SMEs as quasi-equity instruments.

- **Abolishing the 150 000 EUR threshold in COSME**

  The COSME loan guarantee facility provides SME financing up to 150,000 EUR for any type of SME. Above this threshold, which got newly introduced in the current programme period, COSME is only applicable if the SME does not fulfil any of the criteria to be eligible under InnovFin. Since the correspondingly necessary delimitation is not always obvious and is often burdensome, we request to abolish it entirely and to get back to the former status quo of CIP and MAP in order to best comply with SMEs' market needs.

- **Clear statutory regime**

  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 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 that this is possible at the beneficiary level should be avoided.

- **Reporting requirements should be as low as possible**

  The reporting requirements laid down in the legal basis should be as simple as possible preserving the essential principle of proportionality.

- **Greater complementarities and synergies between existing instruments and players**

  Synergies should be pursued at all levels, i.e. regional, national and supranational, in order to align incentives and create "win-win" situations for all players along the guarantee value chain, including public authorities, guarantee institutions, banks, and SMEs.

- **Improved database**

  In order to have all relevant data for monitoring- and evaluation-studies on the economic impact (measured by figures regarding innovation, employment and growth) reliable and comparable data is necessary. AECM and its member organisations are prepared to help in an improved data collection through their networks.

We cordially ask you to take our reflections as explained in this position paper into your kind consideration when carrying out the mid-term review of the EU financial instruments.

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