EUROPEAN
COMMISSION

Brussels, 29.6.2021
COM(2021) 337 final

REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT AND THE COUNCIL

Comprehensive Report to the European Parliament and the Council on the use of the European Fund for Strategic Investments (EFSI) EU Guarantee and the functioning of the European Fund for Strategic Investments (EFSI) Guarantee Fund

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1. Introduction

The European Fund for Strategic Investments (EFSI) was set up in 2015, together with the European Investment Advisory Hub (EIAH) and the European Investment Project Portal (EIPP), under Regulation (EU) 2015/1017 of the European Parliament and of the Council of 25 June 2015, amending Regulations (EU) No 1291/2013 and (EU) No 1316/2013[1] (the EFSI Regulation), with the aim of kick-starting investments in the Union through the mobilisation of private finance. The agreement on the management of the EFSI and on the granting of the EU Guarantee (the EFSI Agreement) was signed by the Commission and the European Investment Bank (the EIB) on 22 July 2015.

The EFSI Agreement was amended and restated several times:

- The **first** amendment and restatement of the EFSI Agreement was signed on 21 July 2016, adding two further Products under the SME Window (SMEW): the SMEW Equity Product and the EaSI[2] Guarantee Enhancement;

- The **second** amendment and restatement of the EFSI Agreement was signed on 21 November 2017, converting the three guarantee Products under the SMEW from a temporary enhancement (frontloading) to a permanent enhancement (top-up) structure and adding a new SMEW Product, the Cultural and Creative Sectors Guarantee Facility (CCS GF) Enhancement;

- In 2017, the EFSI Regulation was amended by Regulation (EU) 2017/2396 of the European Parliament and Council of 13 December 2017 amending Regulations (EU) No 1316/2013 and (EU) 2015/1017 as regards the extension of the duration of the EFSI as well as the introduction of technical enhancements for the Fund and the EIAH[3] (the EFSI 2.0 Regulation). The EFSI 2.0 Regulation increased, *inter alia*, the size of the EU Guarantee and adjusted the provisioning target rate. A **third** amendment and restatement of the EFSI Agreement was signed on 9 March 2018 to reflect the EFSI 2.0 Regulation;

- The **fourth** amendment and restatement of the EFSI Agreement was signed on 20 December 2018 to increase the EFSI contribution to existing SMEW Products and add two further SMEW Products (EFSI Combinations Product and EFSI Private Credit for SMEs Product);

- The **fifth** amendment and restatement of the EFSI Agreement was signed on 27 March 2020 to, *inter alia*, increase the EFSI contribution to the existing SMEW Products and add two new SMEW Products (the European Scale-up Action for Risk Capital (ESCALAR) Product and Skills and Education (S&E) Product);

[1] OJ L 169, 1.7.2015, p. 1-38.
[2] The Employment and Social Innovation programme.
[3] OJ L 345, 27.12.2017, p. 34.

- As a response to contain the economic impact of the COVID-19 virus, the **sixth** amendment and restatement of the EFSI Agreement was signed on 27 April 2020 to repurpose resources from the Infrastructure and Innovation Window (IIW) Equity Portfolio National Promotional Banks (NPBs) as well as certain existing SMEW Products to support working capital lending to companies impacted by COVID-19.

  In this context, the EU Guarantee allocated to the COSME Loan Guarantee Facility (COSME LGF) Enhancement was increased to EUR 1,484 million and the EU Guarantee allocated to the InnovFin SMEG Enhancement was increased to EUR 1,400 million.

Article 18(3)(b) of the EFSI Regulation provides that the Commission shall, by 30 June 2018 and every three years thereafter, publish a comprehensive report on the use of the EU Guarantee and the functioning of the Guarantee Fund.

The EFSI commitment period ended on 31 December 2020. Signatures of the already approved EFSI operations may occur until 31 December 2022, whilst operational monitoring will continue until repayment of all financing and investment operations supported by the EU Guarantee.

The cut-off date for all figures in this report is 31 December 2020.

2. The EU Guarantee

The Union provides an unconditional, irrevocable and first demand guarantee to the EIB for financing and investment operations under the EFSI. By providing higher risk bearing to the EIB, the EU Guarantee allows for an increase in the volume of higher risk projects supported by EIB financing and investment operations under IIW and, as a result, helps addressing market failures and sub-optimal investment situations. The EU Guarantee also allows for a greater volume of lending and a larger number of companies to be covered under the SMEW by the European Investment Fund (EIF) and thereby facilitates access to finance[4] for SMEs and small mid-cap companies.

Part of the overall EFSI operations is covered by the EU Guarantee while a part is carried out at the own risk of the EIB. The initial endowment of the EU Guarantee was of EUR 16 billion from the Union budget, complemented by an allocation of EUR 5 billion of EIB's own resources. These amounts were increased to EUR 26 billion and EUR 7.5 billion, respectively, by the EFSI 2.0 Regulation.

[4] Article 3 of the EFSI Regulation.

The nature of the EU Guarantee is revolving until the end of 2022, meaning that the EU Guarantee cover may be made available to new operations following the amortisation of existing ones, provided that the EU Guarantee never exceeds EUR 26 billion and that aggregate net payments from the general budget of the Union under the EU Guarantee do not exceed EUR 26 billion.

The EU Guarantee covers financing and investment operations signed by the EIB under the IIW and by the EIF under the SMEW. The initial repartition between the two windows was up to a maximum of EUR 13.5 billion for the IIW and up to a maximum of EUR 2.5 billion for the SMEW. Given the strong response to the SMEW, the EFSI Steering Board decided to reinforce the latter through the reassignment of EUR 500 million from the IIW to the SMEW in July 2016. The EFSI 2.0 Regulation further increased the share of the SMEW, setting a limit of EUR 6.5 billion that could be adjusted by the Steering Board up to a maximum of EUR 9 billion[5] (Table 1).

In April 2020, as a response to the COVID-19 pandemic, the EFSI Steering Board approved the transfer of EUR 250 million from the IIW Equity NPBs Portfolio to the SMEW in order to increase the capacity of instruments targeting COVID-19 impacted SMEs.

Table 1 - The split of the EU Guarantee and its development over time

(in billion EUR)	Year	IIW	SMEW	Total EU Guarantee	EIB own resources	Total EFSI
EFSI 1.0	2015	13.5	2.5	**16.0**	5.0	**21.0**
EFSI 1.0 adjustment	2016	13.0	3.0	**16.0**	5.0	**21.0**
EFSI 2.0	2018	19.5	6.5	**26.0**	7.5	**33.5**
EFSI 2.0 adjustment	2020	19.25	6.75	**26.0**	7.5	**33.5**

Source: Commission services

[5] Article 11(3) of the EFSI Regulation.

EFSI response to the COVID-19 crisis

Following the outbreak of the COVID-19 pandemic in early 2020, EFSI was part of the European coordinated response seeking to mitigate the socio-economic impact of the COVID-19 crisis. Based on the resources unlocked from EFSI, the EIF provided guarantees of EUR 2.2 billion to financial intermediaries, making available EUR 8 billion in financing for businesses, including micro and social enterprises as well as SMEs in the cultural and creative sectors.

Furthermore, in order to provide support to final beneficiaries within the fastest timeframes, the EFSI Steering Board decided in April 2020 to simplify the approval process for specific operations within COVID- 19 envelopes of financing under the IIW.

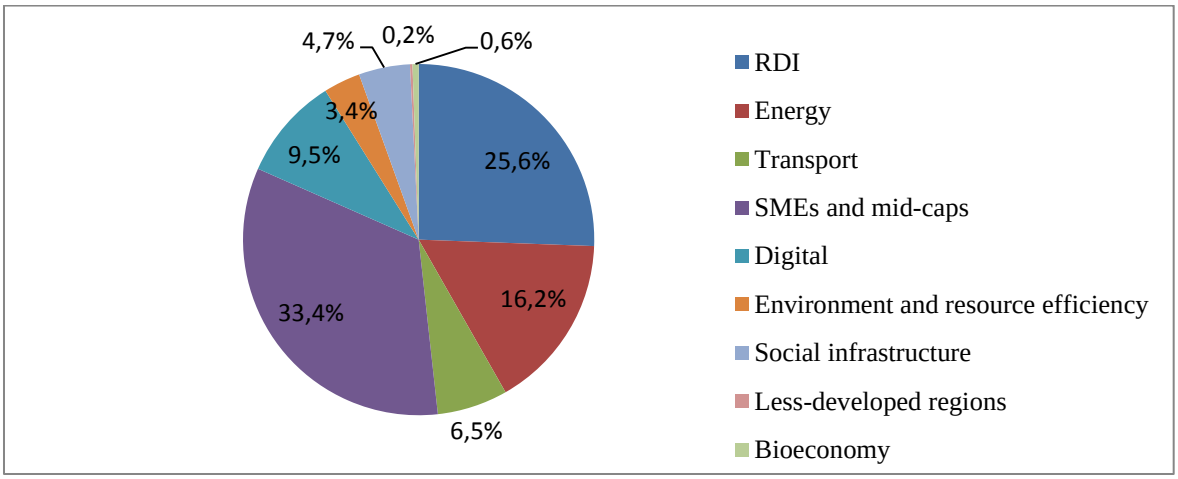
For example, the EIB Board approved in May 2020 the EFSI transaction supporting the German BioNTech SE with EUR 100 million in debt financing for the development and manufacturing of COVID-19 vaccine. This allowed the company to expand its manufacturing capacity in order to supply the vaccine worldwide as fast as possible in response to the pandemic.

3. The use of the EU Guarantee

This section reviews the use of the EU Guarantee under the different activities supported by the EFSI. The EU Guarantee covers different products under the two windows: Infrastructure and Innovation Window and SME Window.

As of end-2020, the EIB group (EIB and EIF) approved 1,549 operations under EFSI for a total financing of EUR 103 billion. Of these operations 1,421 had already been signed as of end-2020, for a total financing of EUR 82.7 billion. The approved operations are expected to mobilise investments of EUR 545.3 billion (of which the total investments of already signed operations amounts to EUR 479.5 billion) in all EU Member States and across all objectives set out in the EFSI Regulation, with more than half allocated to Research, Development and Innovation (RDI) and SMEs and mid-caps (Figure 1).

Figure 1: EFSI investment mobilised for signed operations (by sector, December 2020)



Source: Commission services

At the end of 2020, the exposure of the EU budget to possible future payments under the EU Guarantee in terms of signed operations (disbursed and undisbursed) amounted to EUR 24.1 billion, whereas the overall outstanding disbursed exposure covered by the EU Guarantee amounted to nearly EUR 18.9 billion.

As of 31 December 2020, the EU Guarantee was called under the IIW for the total amount of EUR 80.4 million. In addition, an amount of EUR 5.0 million was called for EIB funding costs, EUR 77.4 million for value adjustments of equity-type operations and EUR 3.9 million for recovery costs and EIB recoverable administrative fees.

As of end 2020, under the SMEW, the EU Guarantee was called for the total amount of EUR 45.6 million which was used to purchase non-EUR currencies for hedging purposes.

3.1. Infrastructure and Innovation Window

Under the IIW, the allocation of EIB operations to the debt or equity portfolio is based on the EIB's system of loan grading and the EIB's standard risk assessment. Under the IIW, the EU Guarantee cap amount of EUR 19.25 billion is broken down as follows:

- up to EUR 15.24 billion for debt-type operations;
- up to EUR 4.01 billion for equity-type operations.

As of 31 December 2020, under the IIW, the EIB signed 629 operations for a total financing of EUR 57.2 billion, which are expected to mobilise investments of EUR 278.2 billion in all Member States.

3.1.1. IIW Debt Portfolio

The IIW Debt Portfolio includes all signed and not cancelled debt-type operations. For each operation, the EIB conducts its standard risk assessment, involving the computation of the probability of default and the recovery rate, without taking into account the EU Guarantee (in order to reflect the overall risk of the transaction[6]). The operations supported by the EU Guarantee typically have a higher risk profile than EIB normal operations and hence fall within the scope of *special activities*[7]. Less risky transactions may be incorporated into the EFSI portfolio, provided that a high added-value is clearly demonstrated and their inclusion is consistent with the criterion of providing additionality.

Under the IIW Debt Portfolio, the Union budget provides a 100 % first-loss piece guarantee for the debt portfolio implemented by the EIB under the EFSI. The first-loss piece is expected to be approximately 25 % for the IIW Debt Portfolio-Standard and 33 % for the IIW Debt Portfolio-Hybrid[8] of the volume of the overall portfolio of operations financed by the EIB at the end of the investment period, whereas the residual risk is fully borne by the EIB.

The EU Guarantee may be called in case of defaults by EIB's obligors or, if a restructuring process is undertaken, to cover restructuring losses in relation to debt-type operations.

EIB debt operations generate revenues established in accordance with EIB pricing methodology. Risk-related revenues are shared between the Union and the EIB on the basis of the risk- and revenue-sharing principles set out in the EFSI Agreement, according to which the EU guarantee covers the full of first-loss piece, whereas the EIB retains the full residual risk tranche.

As of 31 December 2020, 460 debt-type operations, of which 403 debt-standard and 57 debt-hybrid had been signed under the IIW for a total financing of EUR 50.3 billion.

3.1.2. IIW Equity Portfolio

The IIW Equity Portfolio includes all signed and not cancelled equity-type operations. Under this portfolio, the EU Guarantee may be used to support direct investments in individual companies or projects (equity-type direct investments) or financing for funds or analogous portfolio risks (equity-type portfolio).

The EIB performs its standard assessment and determines whether an operation bears equity-type risks or not, irrespective of its legal form and nomenclature.

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6 Annex II of the EFSI Regulation, point 6.

7 EIB Statute, Article 16.

8 A hybrid compartment within the IIW Debt Portfolio was created to accommodate specific operations such as risk-sharing operations, which EIB delegates fully to financial intermediaries, Asset Backed Securities, etc. As of 31 December 2020, the allocation of EU Guarantee to this portfolio was EUR 2 billion.

Under the IIW Equity Portfolio - Standard, the EIB invests on a *pari passu* basis with the EU guarantee. The EU guarantee covers 50% in each equity-type operation included in the IIW Equity Portfolio - Standard, whereas the EIB retains the remaining 50%.

The EU Guarantee may be called to cover negative value adjustments, realised losses at divestment and the EIB funding costs, for the part of the equity investment guaranteed by the EU.

The revenues attributable to the EU guarantee and received in respect of the IIW Equity Portfolio - Standard are used to remunerate the EU Guarantee.

The third amendment and restatement of the EFSI Agreement of 9 March 2018 established an IIW Equity Portfolio - NPBs, in addition to the IIW Equity Portfolio - Standard. On a portfolio basis, the EU Guarantee provides 95% of the first-loss piece, whereas the EIB retains the remaining 5% as well as the full residual risk.

As of 31 December 2020, 169 equity-type operations, of which 163 equity-standard and 6 equity-NPBs had been signed under the IIW for a total financing of EUR 6.9 billion.

3.2. SME Window

The SMEW facilitates access to loan and equity financing for small and medium sized enterprises and, to a limited extent, also small mid-cap companies. It is implemented by the EIF.

The EU Guarantee allocated to the SMEW under the EFSI Regulation is capped at EUR 6.75 billion for both debt and equity operations.

As of 31 December 2020, the EIF signed SMEW operations with financial intermediaries for a total EIF financing of EUR 25.5 billion. These operations are expected to mobilise investments of EUR 211 billion in all Member States. Furthermore, a total of 1,427,600 companies had received EFSI financing under the SMEW.

3.2.1. SMEW Debt Portfolio

In the area of support to loan financing, a part of the SMEW benefitting from the EU guarantee boosts pre-existing EU financial instruments for SMEs. Their enhancement under EFSI allowed for a faster deployment of the guarantee and allowed these financial instruments to support a greater volume of lending and a larger number of companies. Specifically, the support is provided to the following facilities:

- the COSME LGF that enhances access to finance for riskier SMEs;
- the InnovFin SMEG that focuses on innovative and research-intensive enterprises;
- the EaSI Guarantee Facility which supports microfinance and social enterprises;
- the CCS GF which provides dedicated support to SMEs in the cultural and creative sectors;

- the S&E Product that was developed as a pilot under the EFSI and provides financing for individual students and learners, entreprises investing in the re-skilling of their employees and organisations offering/investing in education and training; and
- the EFSI Combinations Product which targets specific policy objectives in Member States, especially enhancing access to finance in the agricultural sector. It combines resources from EU structural funds or national funds and EFSI.

As of 31 December 2020, 437 debt-type operations had been signed under the SMEW for a total financing of EUR 15.1 billion.

3.2.2. SMEW Equity Portfolio

In the area of equity financing, the part of the SMEW benefitting from the EU Guarantee under EFSI supports three facilities:

- the SMEW Equity Product, under which the EIF invests in equity funds, funds of funds or co-investment vehicles that channel equity financing to early stage companies (e.g. start-ups) and growth and expansion stage companies (e.g. scale ups);
- the ESCALAR which helps funds focused on scale-ups to achieve a larger critical mass; and
- the EFSI Private Credit Programme supporting diversified debt funds, thus increasing the volume and diversity of alternative debt financing available to European SMEs and small mid-caps.

Additionally, the SMEW also benefits from a direct EIB contribution of EUR 4 billion which has served to extend the EIB's Risk Capital Resources mandate to the EIF in support of equity financing for SMEs and mid-caps.

As of 31 December 2020, 355 equity-type operations had been signed under the SMEW for a total financing of EUR 10.5 billion.

4. The functioning of the EU Guarantee Fund under EFSI

The Guarantee Fund under the EFSI (the Guarantee Fund) was established under Article 12 of the EFSI Regulation and it is funded mainly from payments from the Union general budget and revenues originating from operations under the EU Guarantee. The Guarantee Fund constitutes a liquidity cushion from which the EIB is to be paid in the event of a call on the EU Guarantee. The Guarantee Fund has to be maintained at a certain percentage (the Target Rate) of the total amount of the obligations under the EU Guarantee, currently set at 35%. Thus, the liquidity cushion is intended to provide an appropriate safety margin avoiding exposing the Union budget to sudden guarantee calls, which could entail spending cuts or budget amendments.

According to the EFSI Agreement, calls are paid by the Guarantee Fund if their amount is in excess of the funds at the disposal of the EIB on the EFSI Account. The EFSI Account, managed by the EIB, was established for the purposes of collecting the Union revenues resulting from operations under the EU Guarantee and recovered amounts, as well as for the payment of calls under the EU Guarantee and for the payment of EIB recoverable administrative costs and recovery costs.

The Financial Regulation[9] established the Common Provisioning Fund (CPF) to hold the provisions assigned to cover the financial liabilities arising from budgetary guarantees and financial assistance programmes under the 2021-2027 Multiannual Financial Framework as well as legacy liabilities. Therefore, as of January 2021, the Guarantee Fund under the EFSI constitutes a separate compartment within the CPF.

4.1. The provisioning mechanism of the Guarantee Fund

The Guarantee Fund is provisioned through:

- contributions from the general budget of the Union; the budget allocated for the Guarantee Fund provisioning amounts to EUR 8,425 million;
- revenues and any other payments received by the Union in accordance with the EFSI Agreement, as well as revenues and repayments from financial instruments under the "Connecting Europe Facility"[10] and "2020 European Fund for Energy, Climate Change & Infrastructure" - Marguerite Fund[11];
- returns (interests) on Guarantee Fund resources invested in the financial markets;
- amounts recovered from projects for which the EU Guarantee was called.

The global provisioning of the Guarantee Fund, as part of the CPF as a compartment since January 2021, is being constituted progressively up until 2022.

4.2. Annual and cumulative flows

The budgetary commitments and payments for provisioning of the Guarantee Fund is presented in Table 2.

Table 2 – Provisioning of the Guarantee Fund

(in million EUR)	2015	2016	2017	2018	2019	2020
Commitments	1,350.0	2,110.2	2,680.3	2,069.3	357.3	301.0
Payments	0	1,018.0	2,489.6	2,013.9	1,166.2	1,248.9

[9] Regulation (EU, Euratom) 2018/1046 (OJ L 193, 30.7.2018, p. 1).
[10] Regulation (EU) No 1316/2013.
[11] Regulation (EC) No 680/2007.

The EFSI commitment period for EU budget contributions ended on 31 of December 2020. Commitments from assigned revenues could be made until 2022, whenever available. As of 31 December 2020, the cumulative amount of approximately EUR 8,868 million were committed for the provisioning of the Guarantee Fund, of which EUR 8,425 million from the EU general budget and EUR 443 million from assigned revenues.

Payments into the Guarantee Fund from the EU budget are scheduled until 2022. However, payments from assigned revenues could be made until 2023. A total amount of approximately EUR 7,937 million was effectively paid into the Guarantee Fund, of which EUR 7,513 million came from the EU general budget, while EUR 424 million was recovered as assigned revenues.

As of 31 December 2020, EFSI operations managed by the EIB under the IIW generated a cumulative net revenue of EUR 674 million for the EU, of which EUR 243 million are related to the year 2020[12].

For the EFSI operations under the SMEW, the EU incurred a cumulative net cost of EUR 452 million, of which EUR 295 million are related to the year 2020[13].

4.3. Composition and key characteristics of the portfolio

The Guarantee Fund's investment portfolio is invested in accordance with the management principles laid down in Commission Decision C(2016)165 of 21 January 2016 approving the asset management guidelines of the guarantee fund of the EFSI.

These guidelines foresee that the assets in the investment portfolio shall provide sufficient liquidity in relation to the potential guarantee calls, while still aiming at optimising the return and risk level that is compatible with maintaining a high degree of security and stability.

Investment and risk management strategies were adopted reflecting the investment objectives and outlook of market conditions. The investment approach aims at enhanced diversification across various fixed income asset classes.

As of December 2020, the investment portfolio was made predominantly of securities issued by sovereigns, sub-sovereigns, supranationals and agencies (46.8% of market value), corporates (20.3% of market value) and covered bonds (17.1% of market value). About 5.2% of the portfolio was invested in liquid and highly-rated (AA/AAA) USD denominated investments. The currency risk exposure of these investments has been hedged.

The portfolio duration at the end of 2020 was 3.19 years and its average credit rating is BBB+.

[12] Figures as per audited Financial Report (Schedule III of EFSI Agreement).
[13] Idem as above.

The bulk of the portfolio is invested in liquid securities and an adequate part (25% of the total portfolio value) matures in less than 12 months.

The profile of the portfolio, in terms of duration, credit risk and liquidity, has been calibrated in line with the forecasted cash-flows arising from the EFSI operations under the EU Guarantee (e.g. projected calls, revenues).

As of December 2020, the proportion of ESG[14]-labeled instruments in portfolio was 9.5%.

4.4. Performance

Performance is calculated on a time-weighted basis in order not to be affected by the size of the portfolio, which grew considerably during the period.

Since its inception in April 2016, the Guarantee Fund delivered an absolute performance of 2.4% as of December 2020. This return was achieved against a background of highly negative rates, especially for what is perceived by the markets as "credit risk free" and liquid exposures in Europe. As an illustration, the 3Y German Bond yield was at -0.77% at the end of 2020.

4.5. Assessment of the adequacy of the Target Rate and the level of the Guarantee Fund

The Target Rate of the Guarantee Fund was originally set at 50% of the total EU guarantee obligations. This target was estimated before the start of EFSI.

In 2016, the Commission's internal evaluation of EFSI[15] concluded that the provisioning of the Guarantee Fund could be adjusted. The risk assessment of the different products supported by the EU Guarantee showed that overall the Union budget would be adequately shielded from potential calls under the EU Guarantee with an adjusted Target Rate for provisioning the Guarantee Fund of 35% taking into consideration recoveries, revenues and reflows from EFSI operations.

The European Parliament and the Council approved the Commission proposal and the Target Rate was set at the level of 35% of the total EU Guarantee obligations as of the entry into force of the EFSI 2.0 Regulation.

The risk assessment of the different products supported by the EU Guarantee in February 2021 confirmed that the overall Union budget would be adequately shielded from potential calls under the EU Guarantee with a 35% target rate, taking into consideration recoveries, revenues and reflows from EIB operations.

[14] Environmental, Social and Governance.
[15] SWD(2016) 297.

5. Conclusions

The latest independent evaluation of the application of the EFSI Regulation that underpinned the Commission's proposal for a Regulation establishing the InvestEU Programme[16] concluded to the overall relevance and effectiveness of the EU Guarantee. In particular, the levels of the EU Guarantee and of the EIB contribution were appropriately sized as it allowed the EIB Group to mobilise a level of investment in line with expectations. The adjustment of the Target Rate for the Guarantee Fund under EFSI 2.0 resulted in a more efficient use of the EU budget. Moreover, the impact on other parts of the EU budget was limited, thereby leading to an increased efficiency of EU budget support. Furthermore, the overall approach to modelling the EFSI Target Rate appeared to be adequate and in line with industry practice.

By end-2020, EFSI triggered EUR 545.3 billion in cumulative investment across all Member States, thus exceeding the EUR 500 billion target while alleviating the impact of COVID-19 on Europe's economy.

In 2021, the Commission will launch an ex-post evaluation of EFSI, which is expected to be transmitted to the European Parliament and Council by end-2022.

[16] SWD(2018) 314 final.