Council of the
European Union

Brussels, 28 January 2015
(OR. en)

DS 1071/15

Interinstitutional File:
2015/0009 (COD)

LIMITE

MEETING DOCUMENT

From:	General Secretariat of the Council
To:	Ad Hoc Working Party on EFSI
Subject:	Commission Services Non-Paper on risk calibration of the EU guarantee under EFSI Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the European Fund for Strategic Investments and amending Regulations (EU) No 1291/2013 and (EU) No 1316/2013

Delegations will find attached the above non-paper.

Commission Services Non-Paper
Risk calibration of the EU guarantee under EFSI

1. Underlying initial assumptions

The EFSI is expected to mobilise additional, riskier investment of up to EUR 315 billion between 2015 and 2017, on top of existing EIB own-resources lending and Union instruments. The initial assumption is that this will be achieved by the provision of EUR 60.8 billion of EIB Group financing to EFSI operations allocated between three different investment windows:

1. Infrastructure and Innovation – Debt window – EUR 44 billion of EIB financing
2. Infrastructure and Innovation – Equity window – EUR 5 billion of EIB financing
3. Support to SMEs window – EUR 11.8 billion of EIB Group financing

The precise level of EIB Group financing will ultimately depend on the demand under the different windows and the risk profile of the operations supported.

The guarantee of EUR 16 billion provided by the EU budget to the EIB Group will support this financing activity by covering a share of the total risk. As detailed below, there is a high likelihood that net losses will not exceed the EUR 8 billion made available by the EU budget under the Guarantee Fund. The EIB will provide EUR 5 billion to EFSI.

The table below provides the summary of the breakdown of the EFSI between the three investment windows under initial assumptions:

In EURbn	Mobilised amount of investment, up to (3 years)	EIB Group financing, up to (3 years)	EU budget guarantee	EIB own funds (cash)	EU budget coverage / EIB Group financing
1. Infrastructure & Innovation – Debt	€ 240bn	€ 44.0bn	€ 11.0bn *(first-loss)*	n.a.	25%
2. Infrastructure & Innovation – Equity		€ 5.0bn	€ 2.5bn *(pari-passu)*	€ 2.5bn	50%
3. Support to SMEs via EIF	€ 75bn	€ 11.8bn	€ 2.5bn (*EIF managed*)	€ 2.5bn	21%
Total	**€ 315bn**	**€ 60.8bn**	**€ 16.0bn**	**€ 5.0bn**	**26%**

2. Impact on the EU guarantee and EU Guarantee Fund

The following sections provide more detailed background as to the assumptions and impact on the EU guarantee and the Guarantee Fund.

a. Infrastructure & Innovation – Debt window

Under the EFSI Infrastructure & Innovation debt window, the EIB would provide debt (e.g. loans or credit enhancement) to eligible projects and companies essentially in the form of senior or junior debt. Such financing would be geared towards more risky projects than what the EIB own lending activity or EU instruments usually support. Such level of risk could be inter alia due to the credit worthiness of the counterparty, the maturity of the financing, the technology risk, concentration risk, country risk or other risks that currently hinder investment in Europe.

The Infrastructure & Innovation Debt window would be supported by a First Loss Piece (FLP) of EUR 11 billion fully covered by the EU budget guarantee.

Under the initial assumptions that the majority of financed transactions are long-dated and more risky than what the EIB usually finances, the EIB would be able to provide up to EUR 44 billion of lending with the backing of the FLP (i.e. EU coverage of at least 25% of the EIB lending to the market). As indicated above the precise level of financing would ultimately depend on the risk profile and maturity of the operations supported (the higher the risk the lower the amount of EIB financing available and vice versa).

According to the proposed Regulation, the risk-sharing revenues attributable to the EU will be made available to increase the level of the Guarantee Fund.

Under the above assumptions, an iterative risk modelling exercise showed that net losses (i.e. losses not compensated by risk-sharing revenues) should not exceed (with a 90% confidence interval) 50% of the first loss piece over a ten-year period. The risk of loss is a function of time and is therefore lower under the current multiannual financial framework period (around 30% of the first loss piece). However, it should be emphasised that the calculations are preliminary and need to be refined in conjunction with the calibration of the risk and investment policies of the fund.

b. Infrastructure and Innovation - Equity window

The total envelope available for equity investments in strategic infrastructure and innovation projects by the EIB has been set to EUR 5bn. The risk will be shared on a pari passu basis by the EIB and the EU guarantee. A pari passu risk sharing is the most efficient approach in terms of consumption of own capital by the EIB on the one hand and risk-alignment between the two risk-sharing partners on the other.

The equity portfolio will target a positive financial return. Building on existing EIB experience based on over EUR 1bn exposure to infrastructure equity funds, while losses can be experienced in individual operations, an overall positive return is expected at portfolio level.

c. Support to SMEs Window

Under this window, the EU and the EIB via EFSI will provide up to EUR 2.5bn each to the EIF, in order for the latter to increase its own activity, under initial assumptions, by up to EUR 11.8 bn.

EIF operations will include equity investments and guarantees to portfolios of SMEs and smaller mid-caps. A part of the EU allocation may be used to frontload existing instruments under COSME and Horizon 2020. While the precise configuration of schemes is currently being developed jointly by the Commission, the EIB and the EIF, the objective is to achieve a broad sustainability of the instruments. The risk calibration will aim at ensuring that losses should not exceed 50% of the capital provided by the EU guarantee.

3. Oversight of risk

According to the proposed Regulation, the Steering Board will determine inter alia the strategic asset allocation and the risk profile of EFSI. In this context, it will have to define an investment policy, a key objective of which will be to determine a risk calibration that ensures the sustainability of the Guarantee Fund.

The Steering Board would also monitor the development of the portfolio and the risk taken by EFSI throughout its implementation and would take appropriate measures in case of need.