OPERATIONS EVALUATION

Evaluation of the EIB Group Risk Enhancement Mandate

September 2020

European Investment Bank
The EU bank

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This publication is related to the following ancillary publications:

- Evaluation of the Social Impact Accelerator, September 2020.
- Evaluation of the Loan Funds Instrument, September 2020.
- Evaluation of the Cooperative Banks and Smaller Institutions Instrument, September 2020.

The main findings of this report have been translated into French and German. They can be consulted at: https://www.eib.org/en/publications/evaluation-of-the-eib-group-risk-enhancement-mandate.

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TABLE OF CONTENTS

Annexes

List of Boxes

List of Figures

LIST OF TABLES

ABBREVIATIONS AND ACRONYMS

ABS	Asset-backed securities
BoD	Board of Directors of the European Investment Bank
CAR	Capital adequacy ratio
CBSI	Cooperative banks and smaller institutions
COSME	The EU programme for the Competitiveness of Enterprises and Small and Medium-sized Enterprises
EA-19	The euro area's 19 members
EaSI	EU Employment and Social Innovation programme
ECA	European Court of Auditors
ECB	European Central Bank
EFSI	European Fund for Strategic Investments
EGF	Pan-European Guarantee Fund
EGFF	European Growth Finance Facility
EIB	European Investment Bank
EIBIS	EIB Investment Survey
EIF	European Investment Fund
EQ	Evaluation question
EREM	EIB Group Risk Enhancement Mandate
ERG	Evaluation Reference Group
ESAF	EIF SME Access to Finance Index
ESIF	European Structural and Investment Funds
ESRB	European Systemic Risk Board
EU	European Union
EU-13	The EU's newer entrants (the 13 countries which have joined since 2004: Bulgaria, Croatia, Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Romania, Slovakia and Slovenia)

EU-15	The EU's earlier entrants (the 15 countries which joined before 2004: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, the Netherlands, Portugal, Spain, Sweden and the United Kingdom)
EU-28	All the Member States of the European Union including the United Kingdom
EV	Operations Evaluation Division of the European Investment Bank
FIs	Financial intermediaries
LFI	Loan Funds Instrument
MC	Management Committee of the European Investment Bank
MFI	Monetary financial institution
MS	EU Member States
NFCs	Non-financial corporations
RSI	Risk-Sharing Instrument
SAFE	Joint European Commission/European Central Bank Survey on the Access to Finance of Enterprises
SIA	Social Impact Accelerator
SIF	Social Impact Finance
SMEs	Small and medium-sized enterprises
ToC	Theory of change
YEP	Youth Employment Programme

KEY TERMS

Additionality	For the purpose of this evaluation, the concept of additionality reflects the basic idea that EIF financing (via EREM) should contribute beyond what is available from other sources. As such, the level of additionality reflects (a) the extent to which a financial intermediary would have been able to obtain the same volume of finance (as the EIF investment) from other sources (public or private) on similar terms and conditions and within the same timeframe; and/or (b) the extent to which EIF financing mobilised capital from other public or private sector entities that would not have otherwise invested in the financial intermediary.
Asset-Backed Securities (ABS) Credit Enhancement Instrument	Under this instrument, the EIF provided guarantees in the context of securitisation, mainly for unfunded (synthetic) or funded (true sale) transactions to increase the ticket size and broaden the scope of the EIB Group's ABS-related activities, from AAA (senior) to BB (mezzanine). The aim was to provide capital relief to financial intermediaries. On the back of this support, financial intermediaries were expected to commit to generating an additional portfolio of loans to SMEs and small mid-caps, as a multiple of the amount of the tranche guaranteed by the EIF.
Capital adequacy ratio (CAR)	The capital adequacy ratio is calculated by dividing a bank's capital by its risk-weighted assets. It is a measure of a bank's available capital with respect to its risk-weighted assets.
Cooperative Banks and Smaller Institutions (CBSI) Instrument	Under this instrument, the EIF provided unsecured senior loans to eligible cooperative banks and smaller financial institutions, for on-lending to SMEs and small mid-caps. The EIB Group did not previously finance this group of financial intermediaries with its own resources due to their small ticket size or low credit rating.
Credit standards	As per the ECB's Bank Lending Survey, credit standards are the internal guidelines or loan approval criteria of a bank. They are applied before negotiations on the terms and conditions of a loan begin and the loan application is approved or rejected.
Final recipients	The ultimate beneficiaries of EIB Group support under EREM such as SMEs, small mid-caps and social enterprises.
Financial intermediaries	Banks or other financial institutions (such as funds, investment companies and leasing entities) through which the EIB Group undertakes its intermediated financing operations.
First-loss piece	The first-loss piece designates the amount which is exposed first to any loss suffered on a portfolio of assets or on a single asset.
Horizon 2020	Horizon 2020 is the EU programme for funding research and innovation. It has a budget of nearly €80 billion of funding available over seven years (2014 to 2020).
Implementation period	The implementation of EREM was envisaged under two periods: • First period: from signature of the EREM agreement (14 March 2014) to 31 December 2016; • Second period: from 1 January 2017 to 31 December 2020. Ultimately, the first period was extended by one year (to 31 December 2017) while the second period did not materialise.

InnovFin financial instruments	Financial instruments under Horizon 2020 are implemented by the EIB Group as part of the InnovFin brand. InnovFin promotes a range of tailored debt and equity products, from guarantees for intermediaries that lend to SMEs to direct loans to enterprises. Moreover, InnovFin provides advisory services, helping support the smallest to the largest research and innovation projects in the European Union and countries associated with Horizon 2020.
Leveraged financing	Leveraged financing is the maximum amount of financing (to be) made available to final recipients, i.e. typically SMEs, small mid-caps and, as relevant, mid-caps. As such, it includes not only EIF financing but also financing made available by other sources (e.g. private investors, financial intermediaries' own resources and national promotional banks).
Leverage	Leverage is calculated as the ratio between the leveraged financing and EIF financing. EIF financing includes EIF resources and resources managed on behalf of its mandators (European Commission, EIB and third parties).
Loan Funds Instrument (LFI)	The LFI contributed to widening the availability of non-bank financing for SMEs and small mid-caps, beyond traditional bank financing, through investments in closed-ended investment funds or other investment vehicles engaged in the business of providing, directly or indirectly, alternative sources of mainly senior, non-distressed debt and/or hybrid debt/equity financing to SMEs and small mid-caps. The LFI envisaged support to: ▪ Selective loan funds: any loan fund which, applying a selective investment approach, invests directly or indirectly in non-banking financing, mainly in the form of non-distressed (a) senior or unitranche (secured or unsecured) loans/bonds and (b) subordinated securities, quasi-equity and hybrid debt instruments, provided that securities under (b) do not represent in aggregate more than 50% of the total capital invested by each selective loan fund. Indicatively, a selective loan fund typically targets a portfolio of between 10 and 30 underlying investments. ▪ Diversified loan funds: any loan fund which, applying a portfolio investment approach, invests directly or indirectly in non-distressed senior (secured or unsecured) financing, mainly in the form of loans, leases and/or bonds. Indicatively, a diversified loan fund typically targets a portfolio of 100 or more underlying investments (including reinvestments).
Managing authority	A managing authority may be a national ministry, a regional authority, a local council, or another public or private body that has been nominated and approved by a Member State to manage and implement EU cohesion funds.
Microfinance Instrument	This instrument was envisaged to represent the EIB Group's senior contribution to the funded product of the EU Programme for Employment and Social Innovation (EaSI). Due to protracted negotiations with the European Commission, the EIB decided to release the €53 million earmarked for the instrument in the first period and develop a microfinance instrument through a different funding source.

Risk-Sharing Instrument (RSI)	The RSI was a guarantee scheme managed by the EIF in the 2007-2013 programming period launched in cooperation with the EIB and the European Commission under the Seventh EU Framework Programme for Research and Technological Development (FP7). The RSI aimed at improving access to debt finance for innovative SMEs and small mid-caps to support their research and innovation projects.
Securitisation	Securitisation is the process of taking an illiquid group of assets, in this case a portfolio of lending to SMEs and small mid-caps, and transforming them into a security through financial engineering.
Signature	Event upon which the EIF signs a finance contract.
Small and medium-sized enterprise (SME)	Micro, small or medium-sized enterprise with a headcount below 250 employees.
Small mid-cap	Enterprise with a headcount of between 250 and 499 employees.
SME Initiative (Option 1 and 2)	Under this instrument, a number of risk-takers mandated the EIF to provide guarantees on their behalf to financial intermediaries which lend to SMEs. The risk-takers were the following, in ascending order of seniority: ▪ European Structural and Investment Funds (ESIF) – first-loss or junior tranche of the Member States and/or managing authorities opting in to the initiative; ▪ European Union (COSME and Horizon 2020) – second-loss or lower mezzanine tranche; ▪ EIB and EIF, under EREM – upper mezzanine tranche; ▪ EIB and/or EIF, under their own resources – senior tranche. The SME Initiative had two products: ▪ Option 1 – portfolio guarantee; ▪ Option 2 – guarantee in the context of securitisation. The final aim under both options was to support financial intermediaries in generating a portfolio of loans to SMEs corresponding to a multiple of the ESIF amount contributed by the Member States and/or managing authorities opting in to the initiative.
Social Impact Accelerator (SIA)	Under this instrument, the EIF provided equity financing to social impact funds targeting social enterprises in Europe.
Youth Employment Programme (YEP)	Under this instrument, the EIF proposed to provide partial guarantees for commercial loans to SMEs and small mid-caps, which in turn created jobs and offered apprenticeships for young people. The aim of the proposed YEP facility was to support youth employment in Europe by building a link between the EIB Group's financing and the employment of young people. YEP – initially envisaged with the EIF at full risk – was eventually not implemented due to the lack of portfolio loss protection from the EIB or other third parties.

Executive Summary

EIB Group Risk Enhancement Mandate

The EIB Group Risk Enhancement Mandate (EREM) was approved by the European Investment Bank (EIB) Board in December 2013 in response to the June 2013 European Council conclusions[1] calling for mobilisation of European resources, including those of the EIB Group, to urgently tackle youth unemployment and support small and medium-sized enterprise (SME) financing. At the time, the EU economy was just emerging from a recession and the future economic outlook remained highly uncertain. The net flow of finance from banks to non-financial corporations was contracting and access to finance for SMEs had deteriorated in several EU Member States (MS), particularly in Eastern and Southern Europe. Moreover, youth unemployment had reached worryingly high levels in some MS, thus becoming a political priority at the EU level.

Against this background, EREM was put together, alongside an increase in the capital base of the European Investment Fund (EIF), to enhance the overall risk-bearing capacity of the EIF. The specific objectives of EREM were as follows:

- To increase access to finance for SMEs and small mid-caps by strengthening the credit enhancement capacities of the EIF and by delivering finance mainly through financial institutions, including guarantee institutions;
- To contribute to the development of European capital market instruments for the benefit of SMEs and small mid-caps;
- To target specific areas in the fields of youth employment; microfinance; cooperative banks and other smaller financial institutions without access to direct EIB financing; social, environmental and innovation impact; and other areas agreed with the EIB.

To achieve these objectives, EREM was allocated a financial envelope of €6 billion over a seven-year timeframe (2014-2020), nominally split 2:1 between the EIB and the EIF. The Mandate was structured in the form of a framework agreement between the EIB and the EIF, under which the Mandate was managed by the EIF on the EIB's behalf on a full delegation basis (except for the CBSI Instrument, which was implemented with shared EIB and EIF responsibilities).[2]

Although the initial design of EREM envisaged the deployment of eight to ten financial products over its lifetime, six products were eventually developed and rolled out between 2014 and 2018. The envisaged implementation of EREM comprised two phases: an initial ramp-up phase covering the 2014-2016 period (first period) and a subsequent follow-on phase from 2017 to 2020 – subject to a review of the first period. Ultimately, the first period was extended by one year while the second phase was dropped to avoid overlaps with the European Fund for Strategic Investments (EFSI), which was launched in 2015 by the European Commission to stimulate investment and included some products similar to those implemented under EREM.

Box 1. Objectives and scope of the evaluation

This evaluation has both summative and formative purposes. It examines how **EREM worked overall as a mandate**, what it achieved and whether the design choices made under the Mandate were appropriate given its objectives. It also identifies a number of lessons learnt and recommendations that may inform the design of future intra-Group mandates or products similar to those implemented under EREM.

Although the evaluation covers the entire Mandate, it focuses primarily on the following three products implemented under EREM: the Social Impact Accelerator (SIA), the Loan Funds Instrument (LFI) and the Cooperative Banks and Smaller Institutions (CBSI) Instrument. Each product is assessed in more detail in accompanying slidedocs. These products are relatively new to the EIF and have not yet been systematically evaluated. As such, evidence is currently lacking on their relevance and effectiveness. Moreover, some of these products are already being taken forward under EFSI and are likely to be scaled up in the future. Ongoing and future activity in these areas can thus draw upon and benefit from the lessons learnt under EREM.

The evaluation covers the 2014-2018 period.

[1] European Council, Conclusions – 27-28 June 2013.

[2] For the CBSI Instrument, loan administration was carried out by the EIB.

Box 2. Methods and data sources

This report is based on:

- An in-depth review of EREM documentation, product-specific documentation and transaction-level documentation;
- A literature review covering specific markets of interest (private debt markets, impact investment markets and financing via cooperative banks);
- Inputs provided by 41 financial intermediaries via online surveys covering the SIA (12/12)[3], the LFI (15/17)[3] and the CBSI Instrument (14/15)[3];
- An online survey of social enterprises receiving financing from SIA-backed funds (42/101)[3];
- Fifteen case studies to test, in different contexts, the assumptions and causal pathways underpinning the theories of change for the SIA, the LFI and the CBSI Instrument;
- Interviews with all relevant EIB and EIF services, 15 financial intermediaries, and eight wider market participants, including investors and intermediaries not involved in EREM;
- Analysis of quantitative data, including Mandate-level financial data, portfolio data for specific EREM products and access to finance statistics;
- A data interpretation workshop with EIB and EIF staff to present, discuss and interpret the data collected, thus ensuring that findings are based on contextual understanding.

Major findings and conclusions

Relevance of objectives and design of the Mandate

The objectives of EREM were quite pertinent to the context in which the Mandate was conceived, but also quite far-ranging in scope and lacking in precision. The Mandate sought to address a number of issues ranging from access to finance to youth unemployment and innovation. Moreover, the Mandate's objectives were not articulated in precise terms: they indicated the direction of travel but not the distance to be travelled.

Eventually, some EREM objectives (and the products initially envisaged to deliver them) were either dropped or pursued through other means. For example, the Youth Employment Programme and the Risk-Sharing Instrument (both originally envisaged under EREM and expected to be fully funded by the EIF) were dropped due to lack of first-loss protection. The microfinance product which was also initially foreseen under EREM was subsequently developed under the EU-funded Employment and Social Innovation (EaSI) programme.

Even so, the final mandate design was quite complex, comprising several novel products. These products either represented new asset classes (e.g. private debt, impact investment) or were targeting new types of financial intermediaries (e.g. CBSI) or final beneficiaries (social enterprises for the SIA). Even some of the relatively straightforward EREM products turned out to be more complex than anticipated. Moreover, the split of financial contributions between the EIB and the EIF added to the complexity of the Mandate.[4]

Consequently, it took a relatively long time (over two years) to develop and deploy some EREM products. The long time to market reduced the relevance of EREM in addressing cyclical gaps in access to finance for SMEs. By the time EREM was launched, financing conditions for businesses had already started improving (primarily due to the accommodative monetary policy of the European Central Bank (ECB)). By the time EREM products reached the market, the cyclical issues in the availability of finance had practically disappeared in most MS, although financing gaps persisted in some MS (e.g. Spain, Greece, Italy, Latvia and Cyprus). Factors outside the EIF's control played some role in delaying the deployment of EREM, but the overly complex design of the Mandate was not particularly well suited to its (implicit) objective of quickly getting money flowing into the real economy.[5]

Nevertheless, some EREM products were still highly relevant to the Mandate's objective of developing non-bank sources of finance for social enterprises, SMEs and small mid-caps. EREM was well designed (in terms of the final product choice) to address this objective. Products such as the SIA and the LFI aimed to develop alternative sources

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3 Number of survey respondents/Number of surveyed counterparts.

4 While the overall risk was nominally split 2:1 between the EIB and the EIF, the distribution of risk could deviate at the product level. Ultimately, risk was split in the ratio of 95:5 for the LFI, the CBSI Instrument and the SIA; 2:1 for ABS Credit Enhancement and the SME Initiative Option 2; and 42:58 for the SME Initiative Option 1.

5 The speed of financing was not explicitly stated as an objective in EREM documentation, but is implicit given the context in which the Mandate was approved and the urgency expressed by the European Council in its June 2013 conclusions.

of finance such as impact investment and private debt for SMEs and small mid-caps, while the CBSI Instrument was designed to enhance the lending capacity of non-bank financial institutions and small cooperative banks.

The strong take-up of some EREM products further illustrates their market relevance. There was strong market demand for the LFI. In response to the high level of market interest for this product, its budget was increased by a factor of six. There was also a strong take-up of products such as the SIA and the Asset-Backed Securities (ABS) Credit Enhancement Instrument. The budget allocated to these products had been fully absorbed by the end of 2018. By contrast, the demand for the CBSI Instrument and the SME Initiative fell short of expectations for various reasons, including design complexity, marketing constraints and factors outside the EIF's control (e.g. the wait-and-see approach adopted by some managing authorities for the SME Initiative).

Effectiveness in enhancing access to finance for SMEs, small mid-caps and social enterprises

By the end of 2019, the EIF had signed deals amounting to €2.2 billion with 112 financial intermediaries located in 21 MS. This contribution from EREM is expected to leverage almost €34 billion[6] of financing for SMEs, small mid-caps and social enterprises over a ten-year period (2014-2023).

The total financing expected to be leveraged by EREM has exceeded expectations. €1 from EREM is expected to leverage €16 of financing for SMEs and small mid-caps, exceeding the indicative leverage of x8 anticipated at the time EREM was approved.

However, there is not sufficient evidence to conclude that this entire volume of financing leveraged is additional. It is possible that part of this financing would have been made available by the market to SMEs and small mid-caps even in the absence of EREM.

To examine this possibility, the evaluation conducted a deep-dive analysis of the additionality of the financing leveraged by the LFI, the SIA and the CBSI Instrument. Over a ten-year period, these three products are expected to leverage €5.7 billion of financing for SMEs, small mid-caps and social enterprises, which is five times the EREM contribution of €1.1 billion (signed volumes). The evaluation finds strong evidence that much of this financing would not materialise in the absence of EREM. Many of the financial intermediaries would not have been able to raise financing from other sources on the same terms and within the same timeframe as the EREM support they received. EIF participation is also found to have played a key role in mobilising capital from other investors, in the case of the SIA and the LFI.

In terms of tangible results achieved so far, EREM financing reached more than 100 000 SMEs, small mid-caps and social enterprises between 2014 and 2019. This represents 54% of the target set for EREM. As the portfolios are still building up, the number of final beneficiaries is expected to rise in the coming years. It is nonetheless clear that the envisaged target number of beneficiaries will not be met for the LFI or the SME Initiative Option 2. For the LFI, the shortfall is explained by the actual average loan size per SME or small mid-cap being much higher than had been initially assumed. This deviation is understandable given that the LFI was a new, untested product for the EIF. For the SME Initiative Option 2, the slow and limited take-up of the product by MS has affected the number of final beneficiaries.

Aside from an increase in the volume of financing available, the assisted businesses have also benefited from improved financing conditions and non-financial support from the LFI, the SIA, the CBSI Instrument and other products. For example, EREM-backed loan funds offer better conditions to borrowers than bank financing, including longer tenors, more flexible financing (e.g. bullet repayment structure) and greater speed of financing (several weeks versus months). Social enterprises prefer SIA-backed funds because they offer better terms and other benefits such as networking. Also, the average maturity of loans offered by CBSI financial intermediaries is longer than that of bank loans.

6 This figure does not include the financing expected to be leveraged by the SME Initiative Option 1 as this information is not available.

Geographical take-up of EREM

Approximately 80% of EREM commitments are concentrated in only six MS (France, Italy, Germany, Spain, the United Kingdom and the Netherlands); these countries represent some 75% of EU gross domestic product (GDP). It is acknowledged, however, that EREM had no specific geographic allocation targets.

There are no EREM commitments in several MS reporting significant access-to-finance gaps, namely Cyprus, Croatia, the Czech Republic, Greece, Ireland, Latvia, Slovenia, Slovakia and Portugal.[7] While some of these countries were well covered by other EIF financing (Croatia, Cyprus, the Czech Republic, Greece, Ireland and Portugal), the other countries (Latvia, Slovenia and Slovakia) have received no EREM financing and a disproportionately low share of overall EIF financing relative to their share of EU GDP and the EU SME population. This can be somewhat explained by factors outside the EIF's control, such as market conditions, lack of market infrastructure, legislative restrictions and, in some cases, lack of a mandate.[8]

The geographic concentration of some EREM products (SIA and LFI) is partly driven by differences in market maturity and the sophistication of financial intermediaries across MS. For these products, the EIF adopted a deliberate and justifiable strategy of initially focusing on countries where the asset class already existed (to build champions and the EIF's own track record and experience), and then diversifying to newer markets (market-building role).

Meanwhile, the CBSI Instrument, which was a relatively plain vanilla product, had limited take-up in many MS with the most pressing SME financing needs. The long delay in launching this product constrained marketing efforts, while eligibility restrictions reduced its attractiveness. It is noted, however, that design constraints under the CBSI Instrument (e.g. sovereign rating) limited the possibility for deployment in some MS.

For the LFI and the ABS Credit Enhancement Instrument, national legislative restrictions also played a role in limiting take-up, while the SME Initiative suffered from the wait-and-see approach adopted by several managing authorities.

Effectiveness in developing non-bank sources of finance for SMEs and small mid-caps

European SMEs are traditionally heavily reliant on bank financing. The financial crisis exposed the weaknesses of this model. Therefore, a key objective of some EREM products (e.g. LFI, SIA) was to develop alternatives to traditional bank-based sources of finance.[9] In support of this objective, EREM has successfully contributed to developing the lower mid-market segment of the European private debt industry (LFI) and the impact investment market (SIA).

The EIF, through its financial investment in intermediaries (via EREM) and signalling effect, has attracted new classes of investors to these asset classes, thus widening and diversifying the investor base. In the private debt sector, the EIF has pulled in institutional investors, public sector investors and high-net-worth individuals. In the impact investment space, there is evidence that the EIF's presence has catalysed investment from family offices, particularly smaller ones.

The EIF has also contributed to developing these markets by means other than investment, such as building new intermediaries (by supporting first-time teams) and strengthening intermediary capacity (by providing structuring support). The structuring input provided by the EIF was appreciated by fund managers and resulted in positive changes. The specific benefits include improved governance of funds (e.g. by addressing conflicts of interest, clarification of roles, issues around team independence and composition) and improved business models (e.g. sharpening of investment focus).

The SIA has also contributed to setting industry standards and best practice in the areas of social impact measurement and performance management, by introducing

7 Based on data available as of December 2018.

8 For instance, the EIF had no mandate for European Structural and Investment Funds (ESIF) in Latvia.

9 This objective was aligned with the Commission's Action Plan on a Capital Markets Union published in September 2015, which sought, for example, to broaden the range of financing options available to businesses.

incentives in the form of impact-based carry.[10]

The evaluation further examined if the impact-based carry mechanism had any influence on the social impact delivered by assisted funds. The evaluation finds no such influence as the assisted funds were already committed to social impact. Nonetheless, the impact-based carry helped to maintain fund managers' focus on social impact and encouraged them to strengthen their monitoring and reporting systems.

Factors affecting efficiency

A few factors affected the efficiency of the Mandate. The launch and deployment of several EREM products was delayed for various internal and external reasons. Internal factors included discussions between the EIB and the EIF regarding the delivery model for the CBSI product, the relatively long time required to sign agreements with financial intermediaries (SIA), and the processes involved in budget reallocations (LFI). External factors included the length of time taken for fundraising (LFI) and the wait-and-see approach adopted by managing authorities (SME Initiative).

The partial delegation model of the CBSI Instrument created several operational challenges and inefficiencies, such as amendments to EIF product documentation in line with the EIB's requirements, manual double entry of transaction data on EIB systems by EIF staff, and the need to split documents and processes to meet the 95:5 capital split requirement. EIB loan administration had to be used to ensure Group-wide consistency regarding lending products. Finally, the evaluation notes that the overall capital consumption of EREM was within the set limits, despite budget shifts to relatively high capital-intensive products.

Recommendations and pointers on what could be done differently in future

Recommendation 1: When designing a mandate, the EIB should:

- Clearly specify the weight assigned to each policy objective if the mandate has more than one. To the extent possible, objective setting should be guided by a SMART[11] framework, clearly defining what success looks like. SMART objectives provide greater focus and a clearer framework for monitoring performance and ensuring accountability.
- Set objectives that are results-based rather than output-focused to ensure flexibility to respond to changes in the context.
- Ensure that the choice of products and budget allocation are aligned with the mandate's hierarchy of objectives. For example, if the objective of an intervention is to quickly get money flowing into the real economy, then it should include a limited number of simple, tried-and-tested, quick-disbursing products, rather than a complex design featuring several new and untested products.

Recommendation 2: The EIB should explicitly set out time-to-market targets for anti-crisis instruments or instruments addressing urgent policy priorities to ensure the timeliness of its response. Accordingly, the governance arrangements and operational processes for the instrument should be designed to facilitate delivery of financing within the established timescales.

Recommendation 3: Provided relevant mandators' resources are made available, the EIF should continue nurturing the development of the lower mid-market segment of the EU private debt industry, which has proven to be a viable alternative channel to bank financing, by supporting diversified loan funds (already ongoing under the Private Credit Programme of EFSI's SME Window) and selective loan funds (currently stalled). There is a strong case for this based on market pull factors (this evaluation found strong demand for the LFI) and push factors (potential adverse effects on levels of bank financing to SMEs due to future regulatory changes, such as the introduction of Basel IV by 2023). If backed by relevant mandators (the EIB, the Commission and MS), future interventions should consider placing greater focus on

[10] Under the impact-based carry mechanism, a fund manager was entitled to receive the carried interest (an additional form of remuneration) only if, in addition to achieving a financial performance which surpassed a predetermined hurdle rate, the fund also achieved certain predetermined social impact targets.

[11] Specific, measurable, achievable, relevant and time-bound.

countries which have only recently implemented a legislative framework for loan fund activity and on countries which have previously not benefited from EIF support. The EIF should consider gradually phasing out interventions in countries where private debt markets are more mature (to avoid market distortion), unless such interventions have a strong rationale (e.g. pan-European platforms) and provided mandators' terms (e.g. as regards sustainability of the mandate) allow for this.

Recommendation 4: The EIF should intensify its marketing and capacity-building efforts to promote take-up of its products in MS where they are most needed. Although geographical take-up of products can be constrained by their demand-driven nature and lack of market infrastructure, where the EIF is entrusted with pan-European mandates, it is important to ensure that EIF support reaches the MS that need it most.

Recommendation 5: Where within its control, the EIF should reduce the time required from the approval of a transaction to contracting. This time has varied significantly between transactions for some EREM products (e.g. SIA) and was often longer than expected. If feasible, some streamlining of procedures and strengthening of legal capacity by the EIF may help to improve efficiency.

Management Response

The Management of the EIB and the EIF welcome the independent evaluation of the functioning of the EIB Group Risk Enhancement Mandate (EREM) conducted by the Evaluation Division.

The EIB Group designed EREM in 2013 in response to a request from the European Council, concomitant with an EIF capital increase, to enhance its risk-bearing capacity to support access to finance for European SMEs and small mid-caps. The objectives of the EREM framework were discussed and designed jointly by the EIB and the EIF, taking into account specific policy areas of high importance for the European Union and the EIB Group.

In December 2013, the Board of Directors endorsed an EIB contribution to EREM of up to €4 billion, to be complemented by €2 billion of EIF resources. The mandate deployment was further framed by a maximum impact on the Bank's regulatory capital (CAR ratio). The EIB and the EIF signed the mandate framework agreement in March 2014.

The comprehensive mandate approach shown in the multi-pronged design of EREM featuring a time-bound, phased implementation of eight bespoke guarantee, debt and equity instruments over seven years (2014-2020) aimed at contributing to the development of (i) European capital market instruments for the benefit of SMEs and small mid-caps; and (ii) specific areas in the fields of microfinance, social, environmental and innovation impact, youth employment, cooperative banks and smaller financial institutions. The instruments thus included the SME Initiative, ABS Credit Enhancement, Loan Funds/Minibonds, Social Impact Finance, intermediated lending to Cooperative Banks and Smaller Institutions, Microfinance, a Youth Employment Programme and a Risk-Sharing Instrument to be defined (the latter three ultimately did not materialise). The initial budget for each period and instrument, with specific co-investment rates between the EIB and the EIF, has been adjusted on several occasions in view of experience gained by the EIF and the actual market demand from financial intermediaries.

After extending the first pilot period (2014-2016) for signatures until mid-2018, the second period (2017-2020) was ultimately not pursued on the basis that it would restrict the Bank's lending volume of high-risk operations and cannibalise the deployment of the European Fund for Strategic Investments (EFSI), which had been launched in the meantime. Under the governance arrangement, EREM operational details were delegated from the EIB Board of Directors to the Management Committee, and implementation was delegated to the EIF.

The evaluation covers the period from 2014 to 2018 and specifically the EREM windows for Cooperative Banks and Smaller Institutions, Loan Funds and Social Impact Finance. It is the result of discussions between the Evaluation Division and EIB and EIF staff working on implementing the Mandate, online surveys and interviews with financial intermediaries and market participants, case studies of financial intermediaries visited to assess the achievement of the Mandate's objectives and desk reviews on all transactions under the instruments in scope.

By assessing the overall functioning of EREM as an intra-Group Mandate and three of its specific instruments, the evaluation offers an opportunity to identify possible lessons learnt and areas of improvement for the functioning of future intra-Group mandates, or even more generally, of products similar to those implemented under EREM. However, the design of EREM and its deployment particularly fit the temporal context as an EIB Group response to the European debt crisis following the earlier global financial crisis.

The report was discussed by EIF senior management and the EIB Management Committee on 26 June 2020 and subsequently by the EIF and EIB Boards on 16 and 17 September 2020, respectively.

Table 1. Recommendations and Management Responses
Recommendation 1: When designing an intra-Group mandate, the EIB should: ▪ Clearly specify the weight assigned to each policy objective if the mandate has more than one. To the extent possible, objective setting should be guided by a SMART[12] framework, clearly defining what success looks like. SMART objectives provide greater focus and a clearer framework for monitoring performance and ensuring accountability. ▪ Set objectives that are results-based rather than output-focused to ensure flexibility to respond to changes in the context. ▪ Ensure that the choice of products and budget allocation are aligned with the mandate's hierarchy of objectives. For example, if the objective of an intervention is to quickly get money flowing into the real economy, then it should include a limited number of simple, tried-and-tested, quick-disbursing products, rather than a complex design featuring several new and untested products.
Management response Agreed ▪ The EIB Management concurs with the recommendation that the design and implementation of intra-Group mandates are to be guided by SMART results-based objectives, rather than merely by overarching policy priorities. ▪ Results-based objectives are agreed as part of a clear intervention logic, defined at EIB Group level. The approach is to be underpinned by an articulate formulation of the overall Group strategies for public policy goals and specific or thematic priorities, as well as a common policy assessment framework for operations. In particular for intermediated finance with an inherently longer project cycle, ex-ante policy assessments are key to guiding mandate design and deployment throughout the implementation period, until the ultimate ex-post results can be assessed in a comprehensive manner. As regards the input, in addition to EIF specialised human resources, market knowledge and institutional capacity, the mandate design should also transparently refer to the required financial resources, notably the EIB Group capital allocation. ▪ Beyond an agreement on results-based objectives and resource allocation, the design of intra-Group mandates should embed an agreed mandate steering mechanism. The set-up should provide assurance that the deployment by the EIF in response to specific market gaps also remains aligned with the overall EIB Group strategy and policy frameworks and continues to fit sustainability, capital and operational business planning in a changing macroeconomic context. Proactive mandate steering will also be appropriate in the context of changing prudential regulation and related EIB Best Banking Practice implementation. Detailed agreement on the EIF activities envisaged under an intra-Group mandate (in terms of products and features, credit risk profile, capital consumption, cost coverage and return on capital) will be opportune to guide and steer its deployment in a changing environment and considering the need for flexibility. In this respect, the design of the EREM – which did include regular task force meetings and a steering committee in its governance structure – provides valuable lessons learnt on which the Group has leveraged in the context of the pan-European Guarantee Fund (EGF) as an EIB Group mandate from the MS. Given the need for close collaboration between the two parts of the Group, a steering group is foreseen in the back-to-back agreement between the Bank and the EIF, in order to facilitate the decision-making process and ensure effective coordination. ▪ Intra-Group mandates require a differentiated approach depending on their objectives and specific macroeconomic context. Mandates designed around a product approach and well-defined "tried-and-tested" product features will be most effective to deliver an immediate EIB Group crisis response. Such an approach was recently endorsed by the EIB Board of

[12] Specific, measurable, achievable, relevant and time-bound.

Directors to deliver on the EGF in response to the COVID-19 crisis, with a specific envelope for the EIF to deliver on (mainly synthetic) securitisation. However, to the extent that mandates are also designed towards longer-term market development objectives, as was the case for EREM, the possibility to pilot new products or market segments should remain an option. The potential roll-out of a product successfully piloted under an intra-Group mandate is to be considered ex-ante and reassessed as part of the periodic review of EIB Group capital and resource allocations.

Recommendation 2:
The EIB should explicitly set out time-to-market targets for anti-crisis instruments or instruments addressing urgent policy priorities to ensure the timeliness of its response. Accordingly, the governance arrangements and operational processes for the instrument should be designed to facilitate delivery of financing within the established timescales.

Management response Agreed

- The EIB Management concurs that intra-Group mandates designed to serve as EIB Group anti-crisis instruments or addressing urgent policy priorities should include time-to-market targets for the EIF. The mandate design should therefore distinguish objectives and differentiate tools and available resources between (i) the acute market gaps for the target beneficiary segment; (ii) any longer-term market or ecosystem development objective; and (iii) the EIF piloting new, alternative products towards its delivery on policy objectives.

- An intra-Group mandate designed around the deployment of “tried-and-tested” products and product features, with clear eligibility criteria in terms of final beneficiaries and intermediaries, will facilitate EIF time-to-market and ensure the relevance of the mandate as a time-limited crisis response. Ex-ante agreement on existing product features will allow reliance on established processes and procedures, thus ensuring operational efficiency, mitigation of operational risk and optimisation of the EIF input. In this respect, the Group has leveraged on the lessons learnt from EREM in the context of the EGF as an EIB Group mandate from the MS.

- In 2019, the Bank adopted an enhanced framework to assess new and existing mandates across the dual dimensions of strategic fit and economic efficiency. The framework also outlines operational measures to improve mandate design and implementation around these dimensions. In 2020, the Bank adopted the revised New Products Policy, the scope of which comprises any mandate identified as a “new product”. The novel character of a mandate is defined by whether its financial structure or implementation framework imply that the EIB is entering into new business areas, is doing existing business in new ways or faces new types of operational risks. The related New Products Policy procedures facilitate the early identification of any operational risk factors that could delay the implementation across different services, also for intra-Group mandates.

- As an alternative to fully-fledged intra-Group mandates, the Bank has also developed intra-Group service level agreements with the EIF. Depending on the specific context and products, such agreements may provide for a more streamlined and flexible approach for the EIB Group to capitalise on EIF technical expertise, human resources and market knowledge in order to quickly deliver a crisis response.

Recommendation 3:
Provided relevant mandators' resources are made available, the EIF should continue nurturing the development of the lower mid-market segment of the EU private debt industry, which has proven to be a viable alternative channel to bank financing, by supporting diversified loan funds (already ongoing under the Private Credit Programme of the EFSI's SME Window) and selective loan funds (currently stalled). There is a strong case for this based on market pull factors (this evaluation found strong demand for the LFI) and push factors (potential adverse effects on levels of bank financing to SMEs due to future regulatory changes, such as the introduction of Basel IV by 2023). If backed by relevant mandators (the EIB, the Commission, and MS), future interventions should consider placing greater focus on countries which have only recently implemented a legislative framework for loan fund activity and on countries which have previously not benefited from EIF support. The EIF should consider gradually phasing out interventions in countries where private debt markets are more mature (to avoid market distortion), unless such interventions have a strong rationale (e.g. pan-European platforms) and provided mandators' terms (e.g. as regards sustainability of the mandate) allow for this.

Management response Partially Agreed

- The EIF concurs with the assessment that it is important to continue nurturing the development of the lower mid-market segment of the EU private debt industry and is committed to providing diversified sources of financing to enterprises beyond traditional banking and through diversified and selective loan funds.

- Currently, the stage of development of the private debt market in the MS is heterogeneous and, in most cases, not yet at the level which would address the alternative funding needs of the final beneficiaries. Legislation across the European Union remains diverse while the establishment of modern frameworks is but one of the parameters that contribute to the development of local ecosystems, fostering the growth of the private debt market.

- The EIF acknowledges that investments under mandates entrusted to it and serving the private debt market can play a key role in aiding the further maturity of such local ecosystems, notably by taking more risks than other investors and acting as a cornerstone investor.

- At the same time, the EIF observes that also for more developed markets, conditions are not present in order to discontinue public interventions. In particular, there remains a need to foster the emergence of additional market participants (first-time teams) but also further the spreading of best market practices. The EIF also notes that it is currently through pan-European funds established in more mature markets that private debt is made available to SMEs and entrepreneurs in countries not benefiting from a home-grown private debt industry.

- For its investments, the EIF is dependent on the specific policy parameters set by mandators (EIB, European Union, MS) and exerts only relative influence on it. In light of the above considerations, the EIF nevertheless expects that future mandates will continue to seek a balanced investment strategy between developed and developing private debt markets, driven by their bespoke policy interests, specific return expectations and the overall economic sustainability of their mandates.

- To the extent policy-oriented mandators do manifest interest in a dedicated focus on markets not traditionally served by existing market operators, the EIF stands ready to provide assistance in order to design bespoke solutions.

Recommendation 4:
The EIF should intensify its marketing and capacity-building efforts to promote take-up of its products in MS where they are most needed. Although geographical take-up of products can be constrained by their demand-driven nature and lack of market infrastructure, where the EIF is entrusted with pan-European mandates, it is important to ensure that EIF support reaches the MS that need it most.

Management response Partially Agreed

- The investment strategy for each particular EIF intervention, including as to geography and desired risk-taking, is driven by the specific policy, return and overall sustainability considerations that are defined by each mandator.

- Many of the EIF's mandates are entrusted to it by individual MS, regions or national promotional institutions, notably through the use of EU Structural Funds. In these cases, the EIF has been in a position to focus on serving local financial markets and developing local ecosystems, such as in the venture capital space. While the EIF offers its structuring expertise for these types of mandates across Europe, it remains the prerogative of relevant decision-makers to seek to engage with the EIF for the deployment of economic programmes.

- For other mandates that have a multi-country geographical remit (as is typical for interventions fostered by central EU mandates or the EIB), EIF products are offered across the relevant territories. At the same time, uptake under mandates is typically subject to market demand with a requirement that the EIF, as an EU body, reviews interest through open and transparent processes (e.g. calls for expression of interest). These elements naturally limit the latitude afforded to the EIF to direct particular mandate intervention towards individual countries or MS. As a European market builder and market developer through pan-European mandates, the EIF perceives its role as fostering an overall ecosystem approach, away from the strict confines of geographical boundaries and national allocations.

- At the same time, in order to live up to the pan-European character of many of its mandates, the EIF engages in strong efforts to develop communication channels and magnify the awareness and the impact of its interventions while calibrating its products accordingly. This approach has enabled it to focus the deployment of mandates in countries where its interventions are most needed. More specifically:
    - In the case of EREM's first objective to increase access to finance for SMEs and small mid-caps, the EIF notes that, when projecting volumes based on the sizes of the respective economies, the countries which were affected more severely by the economic downturn and where it persisted longer (e.g. Spain, Italy, EU-13) benefited substantially more from the support than countries affected less severely by the crisis;
    - In respect of EREM's second objective to contribute to the development of European capital market instruments for the benefit of SMEs and small mid-caps, precisely in order to live up to the need to spread the benefit of EREM's support geographically, two of the instruments (SIA and LFI) were channelled through financial intermediaries typically entailing multi-country investment strategies.

- Finally, with respect to capacity building, the EIF notes its widely recognised role as a provider of structuring inputs and advice to its counterparties, delivering tangible policy benefits to the various market operators in addition to the pure financial parameters of its investments. At the same time, the EIF acknowledges that dedicated capacity-building activities under mandate require a particular resource focus. Developing these aspects of the EIF's delivery will therefore also depend on the willingness of relevant mandators to allocate specific focus and amounts.

Recommendation 5:
Where within its control, the EIF should reduce the time required from the approval of a transaction to contracting. This time has varied significantly between transactions for some EREM products (e.g. SIA) and was often longer than expected. If feasible, some streamlining of procedures and strengthening of legal capacity by the EIF may help to improve efficiency.

Management response Agreed

- The interval between the approval of a transaction and the contract signature itself, which allows the transaction to start deploying its economic benefits, depends on whether it is a debt or equity transaction, whether the intermediary is known to the EIF and whether it is dedicated to the achievement of a number of distinct steps, such as structuring of the investment, fundraising by the financial intermediary to achieve the desired size, marketing of the product, obtaining regulatory approvals and drafting and negotiating the transaction documentation.

- In particular, in the case of many interventions fostered by EREM, the time required from the approval of a transaction to contracting is dependent on two main factors:

  1. In order to crowd in private capital and achieve higher leverage as is required by the mandate and expected of the Fund, the EIF is dependent on the fundraising dynamics deployed by the financial intermediary.

     In the market, the EIF's commitment acts as a "seal of approval" to other investors who can rely on the best practices and thoroughness of the due diligence for which the EIF is known and are hence encouraged to invest in the relevant financial intermediary. However, in order to play this role of cornerstone investor, the EIF is typically among the first investors to approve a particular transaction, before the relevant fund manager focuses on fundraising with other investors. Inevitably, this public policy role of the EIF means that its time between approval and contracting will be longer than that of other investors.

     Moreover, the time taken by fund managers to deploy and complete their fundraising efforts, following approval by the EIF and before proceeding to contracting, is out of the EIF's control. The length of this period will depend on the ability and experience of the fund manager, the then prevailing market conditions and other parameters. For example, in the case of first-time teams or where investments target higher risk and/or policy-driven considerations, relatively more time is required to successfully conclude fundraising.

  2. Living up to its public role, the EIF also provides significant structuring input in view of complying with best market practice. This means that fund structures often need to be revised or sometimes overhauled in the case of an EIF intervention, which can take significant time.

     Notably, requirements stemming from the mandates entrusted to the EIF by the EU, the EIB or MS aimed at achieving best practices or protecting the financial interests of the mandators (e.g. EU Financial Regulation) go – at times – significantly beyond ordinary market standards and need to be explained and translated into contractual provisions through time-consuming and bespoke negotiations. This inevitable feature of the EIF's intervention makes it stand out from other investors, without always being met with full understanding from all market participants.

- Nevertheless, the EIF is continuously making efforts to improve its own efficiency. The time needed for a product to reach the market has been substantially shortened over time as part of the EIF's efforts to address the current market developments in a timely manner. In the case of the most recent products designed to address the COVID-19 crisis, the EIF has deployed novel processes to streamline lead times up to approval and between approval and signature, including standardisation of transaction features, or technological improvements to documentation and signing. Equally, steps are being considered to generally increase delivery capacity, including with a focus on legal resources.

1. INTRODUCTION

The conclusions of the June 2013 European Council[13] called for the mobilisation of European resources – including those of the EIB Group – to urgently tackle youth unemployment and support SME financing, against a backdrop of tenuous economic recovery, falling investment levels, worsening labour market conditions and a declining volume of credit to non-financial corporations (NFCs). In response to the European Council's call, both the EIB Board of Directors (BoD) and the EIF Board approved the EIB Group Risk Enhancement Mandate (EREM) in December 2013,[14] with the objective of enhancing the capacity of the EIF to mobilise financing for SMEs and small mid-caps.

EREM was set up as a mandate from the EIB to the EIF[15] and comprised a series of financial instruments (see below). It was allocated a financial envelope of €6 billion over a seven-year timeframe (2014-2020), nominally split 2:1 between the EIB and the EIF – i.e. the EIB would provide up to €4 billion, to be complemented by up to €2 billion of EIF resources. The envisaged implementation of EREM originally comprised two phases:

- An initial ramp-up phase from 2014 to 2016 with a budget of €2.3 billion (first period);
- A subsequent follow-on phase from 2017 to 2020 (subject to a review of the first period).

Subsequent modifications resulted in the first period of EREM being extended by one year up to the end of 2017 (with the signatures period running until the end of 2018), while the second phase was dropped to avoid overlaps with the European Fund for Strategic Investments (EFSI), which was launched in 2015 and included some products similar to those implemented under EREM.[16]

The initial design of EREM envisaged the deployment of eight to 10 financial products over its lifetime (see **Figure 1**). Ultimately, the following six products were developed and rolled out under EREM over the period from 2014 to 2018:

- **Asset-Backed Securities (ABS) Credit Enhancement:** via this product, the EIF provided guarantees in the context of securitisation, mainly for unfunded (synthetic) or funded (true sale) transactions to increase the ticket size and broaden the scope of the EIB Group's ABS-related activities, from AAA (senior) to BB (mezzanine).
- **Loan Funds Instrument (LFI):** this product took the form of equity investments in funds providing private debt to SMEs and small mid-caps.
- **Cooperative Banks and Smaller Institutions (CBSI) Instrument**: via this product, the EIF provided unsecured senior loans to eligible cooperative banks and smaller financial institutions, for on-lending to SMEs and small mid-caps.
- **SME Initiative**: the EIF offered selected financial intermediaries (e.g. banks, leasing companies, guarantee institutions, debt funds) loss protection and potential capital relief at an advantageous cost. In return for this risk-sharing, the financial intermediaries undertook a commitment to provide SME loans, leasing and/or guarantees at favourable terms (e.g. reduced interest rates and collateral requirements for final recipients). This product comprised two variants: an uncapped portfolio guarantee (Option 1) and a guarantee in the context of securitisation (Option 2).
- **Social Impact Accelerator (SIA):** this involved equity investments in impact funds targeting social enterprises in Europe.

More details on all financial products considered, together with other relevant information on EREM, are provided in Annex 3.

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13 European Council, Conclusions – 27-28 June 2013.
14 The EIF Board approved EREM on 17 December 2013, while the EIB BoD approved EREM on 18 December 2013.
15 The EIB and the EIF signed the EREM Framework Agreement in March 2014.
16 EFSI is the financial pillar of the EU's Investment Plan for Europe and has two components: the Infrastructure and Innovation Window (IIW) managed by the EIB and the SME Window implemented by the EIF. The SME Window has a financial envelope of €5.5 billion to support products targeting SMEs and mid-caps. In its first phase, EFSI was used to deploy existing support for SMEs (under COSME and Horizon 2020) at a higher and faster rate; in its second phase, the EIF scaled up some existing EREM products under EFSI and also developed several new products.

Figure 1. Envisaged products under the EIB Group Risk Enhancement Mandate

Asset-Backed Securities (ABS) Credit Enhancement Instrument	•Product: Guarantees for funded and unfunded securitisation transactions •Counterparts: Financial or credit institutions •Final recipients: SMEs and small mid-caps
Loan Funds Instrument (LFI)	•Product: Equity investment •Counterparts: Selective or diversified private debt funds •Final recipients: SMEs and small mid-caps
Cooperative Banks and Smaller Institutions (CBSI) Instrument	•Product: Unsecured senior loan •Counterparts: Smaller, regionally focused banks and financial institutions •Final recipients: SMEs and small mid-caps
SME Option 1	•Product: Uncapped guarantee •Counterparts: Financial or credit institutions •Final recipients: SMEs and small mid-caps
SME Option 2	•Product: Guarantees for securitisation transactions •Counterparts: Financial or credti institutions •Final recipients: SMES and small mid-caps
Social Impact Accelerator (SIA)*	•Product: Equity investment •Counterparts: Impact funds •Final recipients: Social enterprises
Youth Employment Programme (YEP)**	•Product: Partial guarantees for commercial loans •Counterparts: Financial or credit institutions •Final recipients: SMEs and small mid-caps creating apprenticeships for young people
Risk-Sharing Instrument (RSI) type initiative**	•Product: Guarantee •Counterparts: Financial or credit institutions •Final recipients: Innovative SMEs and small mid-caps
Microfinance Instrument**	•Product: Equity investment •Counterparts: Microfinance institutions •Final recipients: Micro enterprises

* *The SIA was set up prior to EREM as a pilot, combining resources from the EIB Group (95%) and external investors (5%), including Crédit Coopératif, Deutsche Bank, the Finnish group SITRA and the Bulgarian Development Bank (BDB). EREM funding was used to significantly scale it up.*

** *These products were ultimately not implemented under EREM.*

Source: EV

The specific budgetary allocations were initially based on each product's expected market demand, time to market delivery and capital consumption.[17] Because the initial budgetary split across the products did not correspond to the actual market demand experienced during the first period, budgets were reallocated between the products.

[17] The overall capital consumption of EREM was capped at a CAR impact of 0.5%.

The EREM Framework Agreement envisaged full delegation from the EIB to the EIF.[18] However, in practice there was a partial delegation for the CBSI Instrument, with loan administration carried out by the EIB. The overarching principles for EREM collaboration and implementation were:

- Complementarity with EIB and EIF products: there should be no overlap or crowding out of existing EIB Group offers;
- Efficient leverage of EIF expertise, products, systems and procedures, particularly in the areas of assessing and structuring granular portfolios;
- Coordination and cooperation between the EIB and the EIF aimed at:
  - Coherent risk management across the Group;
  - Coherent client relationship management across the Group, especially for common transactions where the EIB already had a relationship with the counterparty.

The following bodies have collaboration and coordination responsibilities for EREM activities: (i) a High-Level Steering Panel; (ii) the EREM Task Force; and (iii) EIB Ops Geographical Departments and/or global relationship managers and the EIF equivalents.

This evaluation examines how EREM worked, what it achieved and whether the design choices made under the Mandate were appropriate given its objectives. It also identifies a number of lessons learnt and recommendations that may inform the design of future intra-Group mandates[19] or of products similar to those implemented under EREM. Specifically, the evaluation offers the first comprehensive evidence and insights on the effectiveness of some relatively new EIF products, such as the SIA and the LFI. These products have been scaled up under EFSI and are also expected to be implemented in some form under the InvestEU Programme.

The remainder of the main report is structured as follows:

- Section 2 sets out the objectives and scope of the evaluation. It also provides an overview of the methodologies used to build a rich and robust evidence base for the evaluation.
- Section 3 assesses the relevance of EREM objectives and whether the design of the Mandate was appropriate given its objectives.
- Section 4 assesses the effectiveness of EREM in achieving its objective of enhancing access to finance for SMEs and small mid-caps.
- Section 5 examines the role and contribution of specific EREM products (namely the SIA and the LFI) in developing non-bank sources of finance for social enterprises, SMEs and small mid-caps.
- Section 6 assesses the factors affecting the efficiency of the Mandate.
- Section 7 presents the conclusions and recommendations of the evaluation.

The main report is supported by the following annexes:

- Annex 1 provides a detailed description of the evaluation methodology.
- Annex 2 contains a list of references used for the evaluation.
- Annex 3 provides additional information on EREM background and theories of change.
- Annex 4 contains supporting data for some of the figures presented in this report.

[18] Under the EREM Framework Agreement, the EIB delegates to the EIF the origination, due diligence, structuring, monitoring, servicing, work-outs as well as pricing and rating of the underlying transactions. For a number of EREM instruments, the EIB retained a non-objection right, yet generally only EIF Board approval is sought for the approval of a new transaction.

[19] In this evaluation, an intra-Group mandate refers to a mandate from the EIB to the EIF.

2. EVALUATION OBJECTIVES, SCOPE AND METHODOLOGY

2.1 Objectives and scope of the evaluation

This evaluation serves summative and formative purposes. It takes stock of what has been achieved under EREM, thus providing accountability for the resources invested. It also examines the design and implementation of the Mandate with the aim of understanding what works and capturing the lessons learnt from the EREM experience.

Although the evaluation covers the entire Mandate, it focuses primarily on the SIA, the LFI and the CBSI Instrument. The reasons for focusing on these products are as follows:

- These products are relatively new to the EIF and have not yet been evaluated. As such, systematic evidence is currently lacking on these products' relevance and effectiveness. Conversely, there is already considerable evidence on the EIF's securitisation activities,[20] so it was decided not to focus on the ABS Credit Enhancement Instrument. The SME Initiative was also excluded from the central scope of the evaluation as it is due to be evaluated by the Directorate-General for Regional and Urban Policy and some MS. Moreover, EREM's contribution to the whole SME Initiative is relatively small (less than 5%).
- The EIF's Corporate Operational Plan for 2018-2020 specifically identifies social impact as an area which should be scaled up, and debt funds as an area where further opportunities should be explored.
- Although the CBSI Instrument is a relatively standard lending product, it is nevertheless an interesting candidate for this evaluation as it represents the EIB Group's first financing of these types of counterparties (cooperative banks and smaller institutions) at the Group's own risk. Moreover, as the launch of the CBSI Instrument was delayed and its implementation created operational challenges, this product offers potentially useful lessons on issues such as coordination and cooperation between the EIB and the EIF.

The evaluation covers the 2014-2018 period, which is the full lifecycle of the first period of EREM. The sampling for fieldwork and detailed analysis of the SIA, the LFI and the CBSI Instrument is based on data up to 31 December 2018. High-level data on EREM signatures, disbursements and the number of final beneficiaries is based on a cut-off date of 31 December 2019. As disbursements are expected to carry on until at least 2023,[21] the disbursed amounts and the number of final beneficiaries will increase over time.

2.2 Evaluation design

The evaluation was designed to respond to a list of evaluation questions reflecting the objectives and scope of the evaluation, the information needs of the primary users of the evaluation (EIB and EIF services) and the key issues meriting further enquiry (as identified through desk research and scoping interviews).

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20 EIB and EV, Evaluation of the EIF's SME Securitisation Activities, 2004-15, 2017. See also European Commission evaluations, e.g. ICF GHK, Evaluation of EIF own resources activity, 2012.

21 This is because a fund's investment period can last up to five years. For the CSBI Instrument, the availability period for disbursements is up to three years (from the date of signature).

Table 2. Evaluation questions

Criteria	Evaluation questions	Scope	Report section
Relevance	EQ1 Were the Mandate objectives relevant and appropriate given the economic context and financing conditions facing SMEs, social enterprises and small mid-caps at the time?	EREM overall	Section 3
	EQ2 Was the design of the Mandate appropriate given its objectives?	EREM overall	Section 3
Effectiveness	EQ3 To what extent has EREM contributed to enhancing access to finance for social enterprises, SMEs and small mid-caps during 2014-2018?	EREM overall (with specific focus on the SIA, the LFI and the CBSI Instrument)	Section 4
	EQ4 Has EREM played a role in shaping and building markets for social enterprises, small mid-caps and SME finance?	SIA and LFI	Section 5
	EQ5 To what extent has the design and implementation of the SIA contributed to the achievement of social impact?	SIA	Section 5
Efficiency	EQ6 To what extent was EREM developed and implemented in an efficient manner?	EREM overall	Section 6

Source: EV

An evaluation matrix was developed during the inception phase of the assignment to guide the choice of specific research methods, as well as to provide a framework for subsequent data analysis and interpretation. The matrix sets out the evidence required to address each evaluation question, the data sources and methods used for compiling the required evidence, and the judgement criteria on which the evaluative conclusions are based.

The overall design of the evaluation reflects the following approaches:

- **A theory-based approach to get inside the "black box" and understand the mechanisms leading to observed outcomes.** This involved making explicit the underlying theory of change (ToC) for each of the three products that are the main focus of this evaluation (LFI, SIA and CBSI Instrument), and subsequently testing these theories to draw conclusions on whether and how EREM contributed to observed outcomes.
- **Using mixed methods to enhance the depth and breadth of the evidence base**. A combination of quantitative (e.g. surveys and statistical data analysis) and qualitative research methods (e.g. interviews, documentation and literature review) were used to gain a deeper understanding of the evaluation issues and to build a more complete evidence base for the evaluation. Mixed methods allow for complementarity (elaborating or clarifying the results from one method with the findings from another method), development (using results from one method to help develop the use of another method) and expansion (extending the breadth and range of inquiry by using different methods for different inquiry components).
- **Triangulation to improve the validity and reliability of the findings.** Multiple lines of inquiry and evidence were used for answering each evaluation question. This provided the basis for cross-checking the information collected from different sources, thus reducing bias. The process of triangulation also helps to generate richer, more nuanced findings by combining multiple perspectives and deepening understanding of an issue.

2.3 Methods and data sources

A range of methods and data sources were used to build a rich and robust evidence base for the evaluation (Figure 2). These are briefly described below; for a more detailed description of each method, see Annex 1.

Figure 2. Methods and data sources used for the evaluation

Source: EV

In-depth review of documentation and literature covering three different levels: Mandate, products and transactions

Mandate-level research included a review of all official documentation relating to EREM set-up and implementation, such as the:

- EREM Framework Agreement;
- Documentation presented to the MC (e.g. requests for budget reallocations);
- Requests for approval submitted to the BoD and the EIF Board;
- EIF reports on the implementation of the Mandate;
- Mid-term review and closure reports.

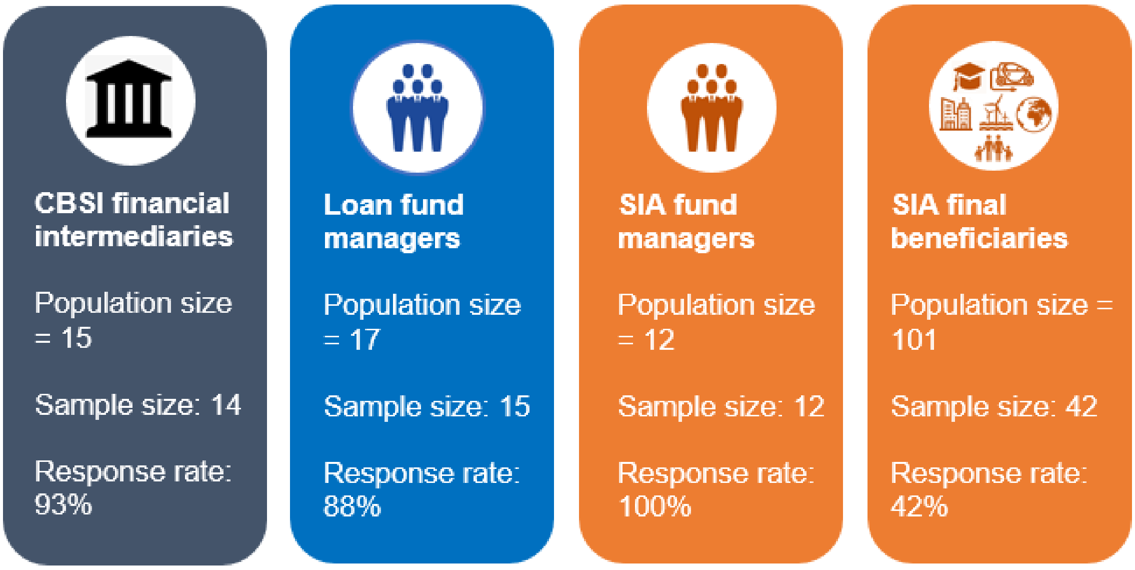
Product-level research included specific product-level agreements signed between the EIB and the EIF and product-specific reporting by the EIF. A literature review was also conducted to understand the evolution of specific markets (private debt markets, impact investment markets and financing via cooperative banks) during the evaluation period.

Finally, transaction-level documentation (e.g. due diligence reports, independent opinions, requests for approval, agreements, side letters, contracts between the EIF and financial intermediaries, as well as any amendments) was reviewed for all transactions financed under the SIA, the LFI and the CBSI Instrument.

Four online surveys to collect structured inputs from financial intermediaries and final beneficiaries for the SIA

Annex 1 provides further details on how the sample frame for the social enterprises survey was constructed.

Figure 3. Overview of online surveys



Note: Population size as of 31 December 2018.

Source: EV

A series of in-depth exploratory interviews with relevant stakeholders to collect their inputs and perspectives

The evaluation team consulted all relevant EIB and EIF staff, 15 financial intermediaries, and eight wider market participants, including investors and intermediaries who were not involved in EREM.

Case-based contribution analysis to test the theories of change for the LFI, the SIA and the CBSI Instrument

The theory of change for each of these three products was tested using a contribution analysis framework. For each product, five intermediaries were selected to test the assumptions and causal pathways underpinning the applicable ToC in different contexts. The contribution analysis was based on a triangulation of evidence collected through missions, surveys and desk research.

Analysis of a range of quantitative datasets

This included an analysis of Mandate-level financial data (approvals, signatures and disbursements), portfolio data for specific EREM products and contextual data on access to finance (EIB Investment Survey (EIBIS), ECB SAFE survey, EIF SME Access to Finance Index (ESAF), monetary financial institution (MFI) lending statistics, etc.).

A data interpretation workshop to collectively interpret, validate and further explore the emerging evidence

This workshop was organised with relevant EIF and EIB staff involved in the design and implementation of EREM to validate the data collected, as well as provide context and additional layers of insight into the evaluation findings. The discussion also provided a basis for identifying the most meaningful findings and added to the depth and accuracy of the analysis. This report reflects the discussions at the workshop.

2.4 Strengths and limitations of the evidence base

The evidence collected for this evaluation has some limitations. These are discussed below:

Lack of final beneficiary perspectives for the LFI and the CBSI Instrument. For logistical reasons (e.g. lack of contact details, language barriers, schedule of the evaluation), it was not feasible to collect inputs from the final beneficiaries of these two products. The evaluation thus lacks final beneficiary perspectives on issues such as the relative advantages of CBSI financing over other sources of financing, and whether they would have been able to secure financing from alternative sources had they not received loans from EREM-backed financial intermediaries.

Low response rate to the survey of social enterprises. The number of responses received was too small to be statistically representative. Due to the risk of non-response bias, the evaluation uses these survey results only as a complementary source of information.

Limited number of interviews with wider market participants (investors and non-assisted financial intermediaries). Only eight of the 50 market participants selected for interviews participated in the evaluation (representing the private debt industry and impact investment markets). Wider market perspectives on the signalling effect of the EIF's intervention are, therefore, not fully represented in this evaluation.

Notwithstanding the above limitations, the overall evidence base for the evaluation is rather strong and robust. This is because:

- The evaluation team had access to large volumes of documentary evidence and factual data on EREM take-up, capital mobilised, etc.
- The high response rates to financial intermediary surveys make these a rather reliable source of information for the evaluation.
- The interviews undertaken with financial intermediaries were rich and informative.
- The range of applied methods permitted multiple lines of inquiry and evidence to answer each evaluation question (triangulation).
- The evidence emerging from the different sources was rather consistent.

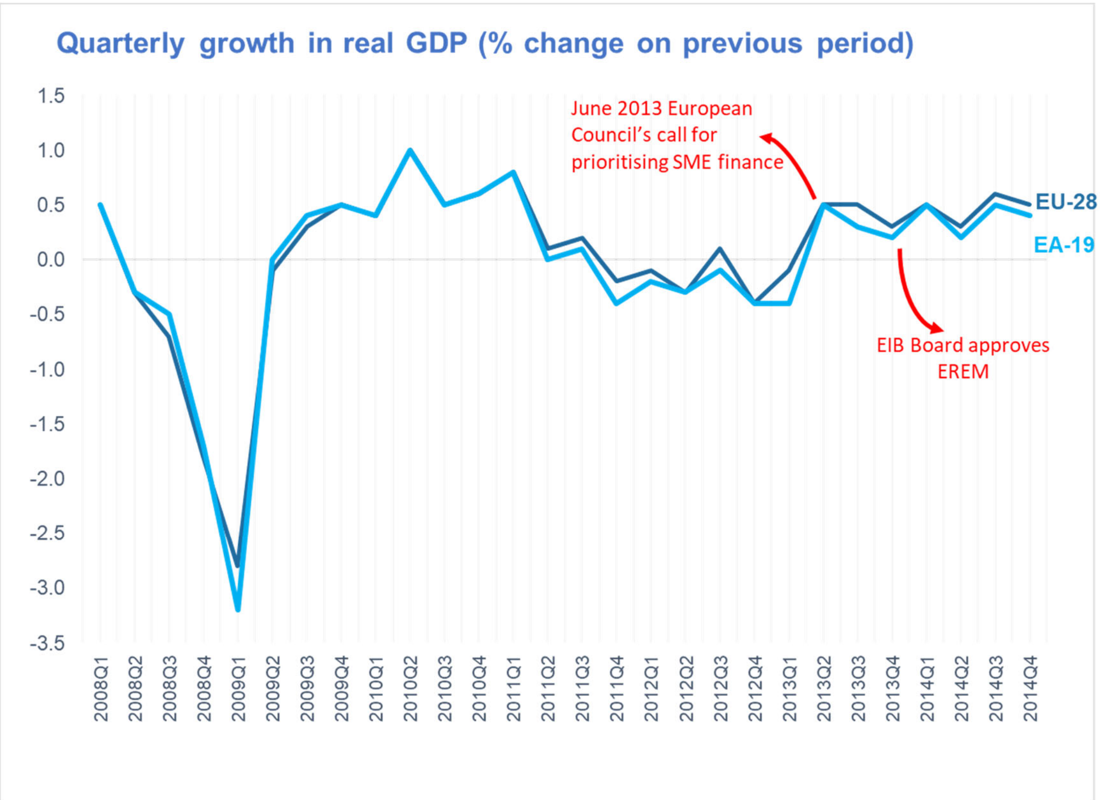
3. RELEVANCE OF EREM OBJECTIVES AND DESIGN

This section examines the extent to which the Mandate objectives were relevant considering the economic context and financing conditions facing SMEs, social enterprises and small mid-caps at the time EREM was designed. It also assesses the extent to which the product choices made under the Mandate were appropriate given its objectives and the wider economic conditions.

3.1 EREM objectives: pertinent but wide-ranging, too ambitious and imprecise

EREM was conceived in 2013 against a backdrop of fragile economic recovery, declining bank lending and high levels of youth unemployment. In June 2013, when the European Council called for the mobilisation of EU resources to support SMEs and boost financing of economic activity, the EU economy was just emerging from a recession (Figure 4) and the future outlook remained highly uncertain. At the same time, the net flow of finance from banks to NFCs was contracting, reflecting both credit demand and supply factors, including stricter regulation and supervision (Figure 5). Access to finance for SMEs deteriorated in several countries after the crisis, particularly as a result of higher interest rates and greater demand for collateral.[22] The deterioration was more significant in the hard-hit countries of Southern Europe.

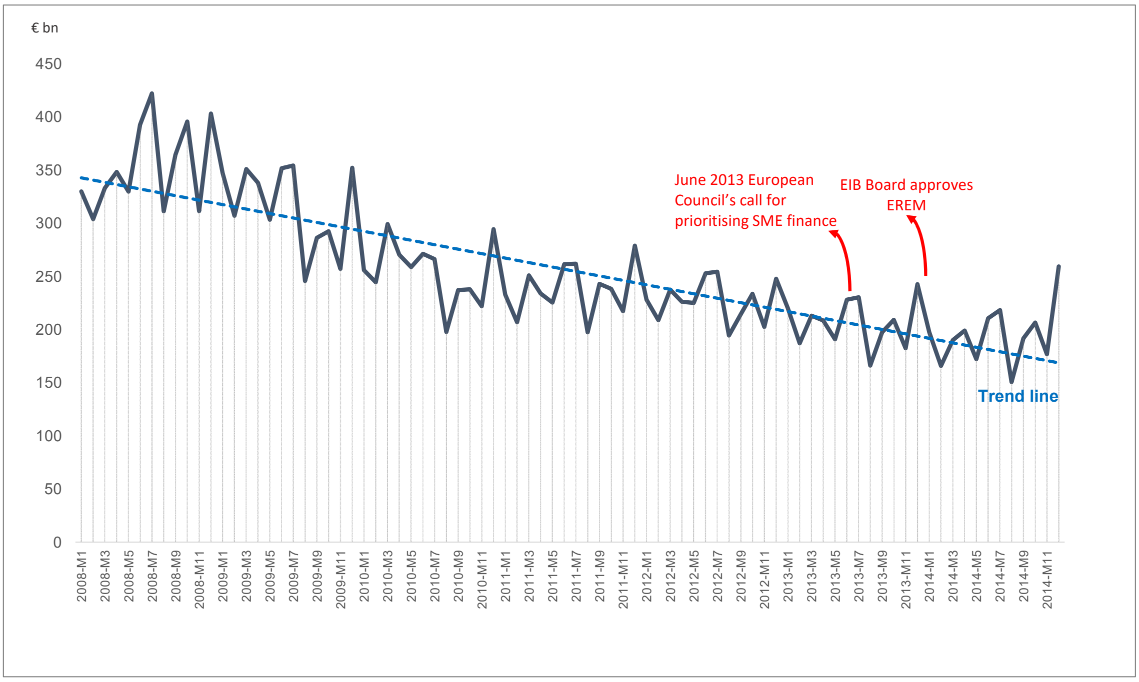
Figure 4. Weak economic growth in the European Union following the recession



Source: Eurostat, seasonally adjusted data

22 Organisation for Economic Co-operation and Development, *Financing SMEs and Entrepreneurs 2013: An OECD Scoreboard*.

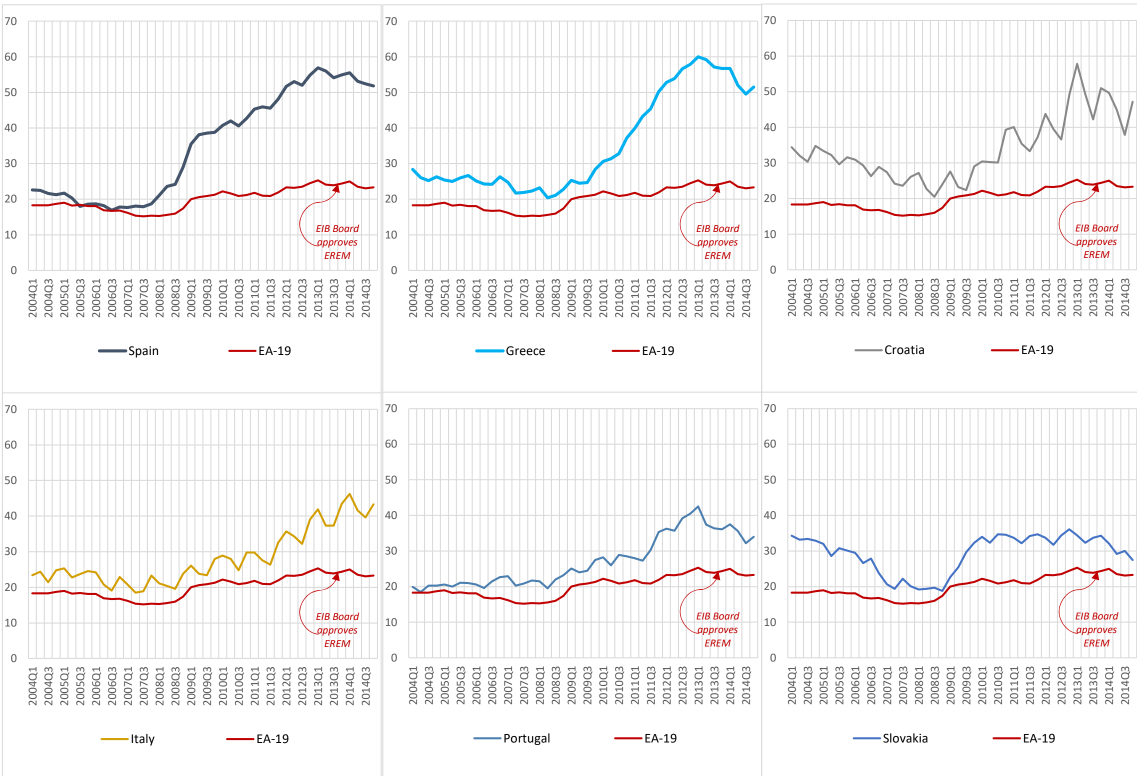
Figure 5. Declining levels of MFI lending to NFCs in the euro area (€ bn)



Source: ECB
Credit and other institutions (MFIs except monetary market funds and central banks) – Loans (new business) other than revolving loans and overdrafts, convenience and extended credit card debt.

Moreover, youth unemployment had reached worryingly high levels in some MS (Figure 6), thus continuing to be a political priority at an EU level.

Figure 6. Youth unemployment levels (%) in selected MS



Source: Eurostat

In the above context, EREM objectives were highly pertinent although quite wide-ranging in scope. The stated objectives of the Mandate (Box 3) were somewhat disparate and aimed to tackle too many issues, ranging from access to finance for businesses to enhancing microfinance and reducing youth unemployment. Ultimately, it was not feasible to pursue some of the objectives via the EIB Group's own resources, e.g. youth employment and microfinance. This led to some Mandate objectives (and product ideas) being either dropped or eventually pursued through other means, so as to optimise capital consumption and avoid overlaps with other products. For example, the Youth Employment Programme and the Risk-Sharing Instrument (both originally envisaged under EREM and expected to be fully funded by the EIF) were not developed by the EIF due to the lack of first-loss protection and to avoid overlap with other EIB Group risk-sharing products further rolled out under EFSI. A microfinance product which was also initially envisaged under EREM was subsequently developed under the EU-funded Employment and Social Innovation (EaSI) programme.

Moreover, EREM objectives were lacking in precision. Given the context in which EREM was conceived, an implicit objective of the Mandate was to quickly get money flowing to SMEs and small mid-caps. The Mandate also had structural objectives (objectives 2 and 3). However, there was no clear hierarchy or explicit prioritisation of these objectives. Moreover, the Mandate objectives were not well defined. Objectives should ideally reflect a sensible goal-setting framework guided by SMART[23] criteria. As such, objectives should specify what should be achieved by when and be measurable to the extent possible. However, EREM objectives were articulated in the form of directional statements (or, in the case of objective 3, just descriptions of topic areas), rather than as specific targets or in terms of the distance to be travelled. Lack of precision also makes it difficult to assess whether or not an objective has been met.

Box 3. Mandate and product-specific objectives

EREM objectives as per the Framework Agreement:

1) Increase access to finance for SMEs and small mid-caps by strengthening the credit enhancement capacities of the EIF and by delivering finance mainly through financial institutions, including guarantee institutions;
2) Contribute to the development of European capital market instruments for the benefit of SMEs and small mid-caps;
3) Target specific areas in the fields of youth employment; microfinance; cooperative banks and other smaller financial institutions without access to direct EIB financing; social, environmental and innovation impact; and other areas agreed with the EIB.

Product-specific objectives

SIA: Extend the EIF's offer of funding instruments to operators in the social economy.

CBSI Instrument: Contribute to widening the availability of small bank and non-bank financing for SMEs and small mid-caps, beyond traditional bank financing, through the EIF granting loans in eligible currencies to eligible cooperative banks and smaller financial institutions.

LFI: Contribute to widening the availability of non-bank financing for SMEs and small mid-caps, beyond traditional bank financing, through investments in loan funds.

ABS Credit Enhancement: Enhance the impact of the EIB Group by achieving a scalable effect in the SME securitisation market, in terms of SME financing and capital relief for the originating financial institution (by enabling the EIF to credit enhance larger securitisation tranches) and, in turn, creating extra capacity to lend to SMEs.

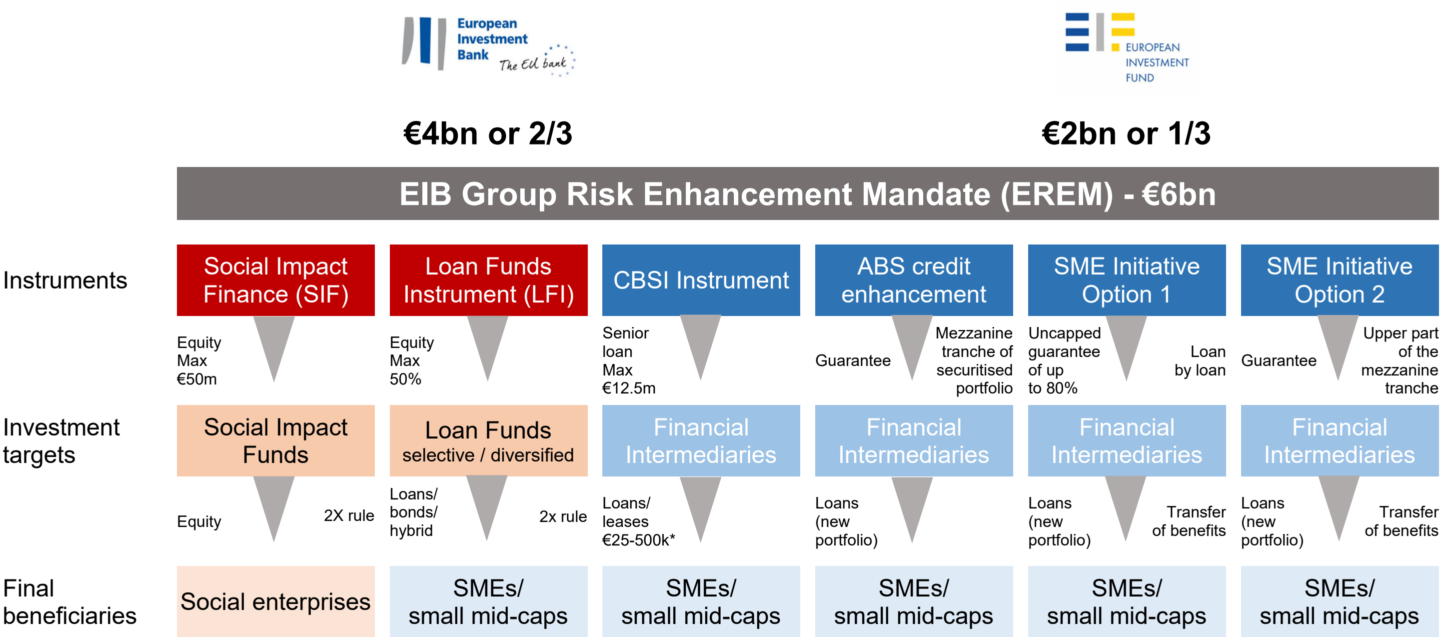
SME Initiative: Stimulate the provision of new debt finance for SMEs by financial intermediaries targeting, for example, finance for SMEs' establishment and early growth phase, the expansion and strengthening of general activities, the realisation of new projects, and penetration of new markets or new developments by existing enterprises in the relevant MS.

[23] Specific, measurable, achievable, relevant and time-bound.

3.2 EREM design: a complex structure comprising several different products

The final design of the Mandate was quite complex (Figure 7). It included a broad range of products (a mix of funds, senior loans, different types of guarantees and securitisation products), each with its own features and rules. For example, the SIA had specific requirements for funds relating to social impact measurement, as well as an impact-based carry methodology which linked carried interest to the achievement of predefined social impact targets.[24] Some products such as the SIA and the LFI envisaged the provision of "structuring input",[25] while others did not.

Figure 7. Structure of the EIB Group Risk Enhancement Mandate



* *loans < €25 000 only eligible if they are covered by an EaSI guarantee.*

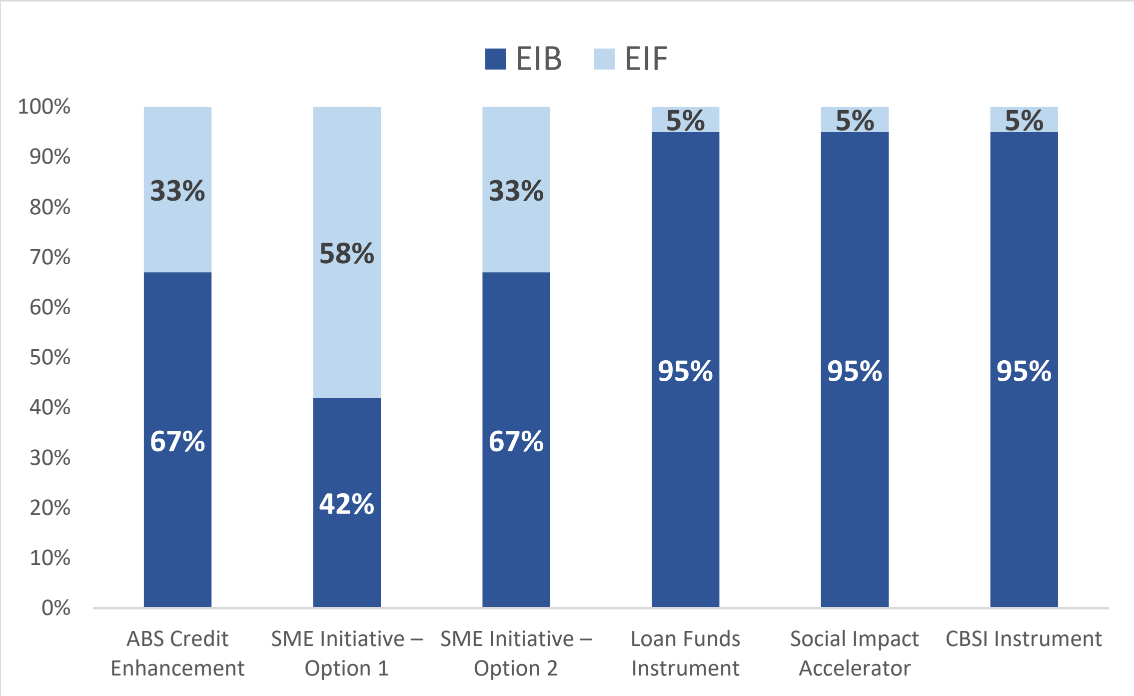
Source: EV

The split of financial contributions between the EIB and the EIF also added to the complexity of the Mandate (Figure 8)**.** While the overall risk was nominally split 2:1 between the EIB and the EIF, the distribution of risk could deviate at the product level.

[24] Fund managers would only receive the carried interest (i.e. more money) if, in addition to achieving financial performance above a hurdle rate, they also reached the predefined social impact target.

[25] In terms of structuring input, the EIF assists fund managers in fine-tuning their investment strategies, including through positioning in relation to current and future competition. The EIF may also contribute to aligning interests between investors and managers, for example by increasing the management team's commitment and optimising the composition of management boards.

Figure 8. EREM distribution of risk



	EIB	EIF	Budget (€ m)
ABS Credit Enhancement	67%	33%	855
SME Initiative – Option 1	42%	58%	245
SME Initiative – Option 2	67%	33%	250
Loan Funds Instrument	95%	5%	1 053
Social Impact Accelerator	95%	5%	189
CBSI Instrument	95%	5%	195
EREM Total	**79%**	**21%**	**2 787**

Source: EV adapted from EIF

Moreover, EREM included several novel products, either representing new asset classes (e.g. private debt/loan funds, impact investment) or targeting new types of intermediaries (e.g. CBSI) or final beneficiaries (social enterprises through the SIA).

Some products were intrinsically complex. For example, the SME Initiative was initially designed as a pan-European initiative, but as the initial design was not taken up by MS, the product was eventually offered on a country-by-country and region-by-region basis. The product turned out to be quite complex due to the involvement of several risk-takers[26] (the EIB, the EIF, managing authorities and the European Commission) and its capital and regulatory structure.[27]

Even some of the relatively straightforward EREM products turned out to be more complex to launch than anticipated. For example, the CBSI Instrument – a relatively plain vanilla product

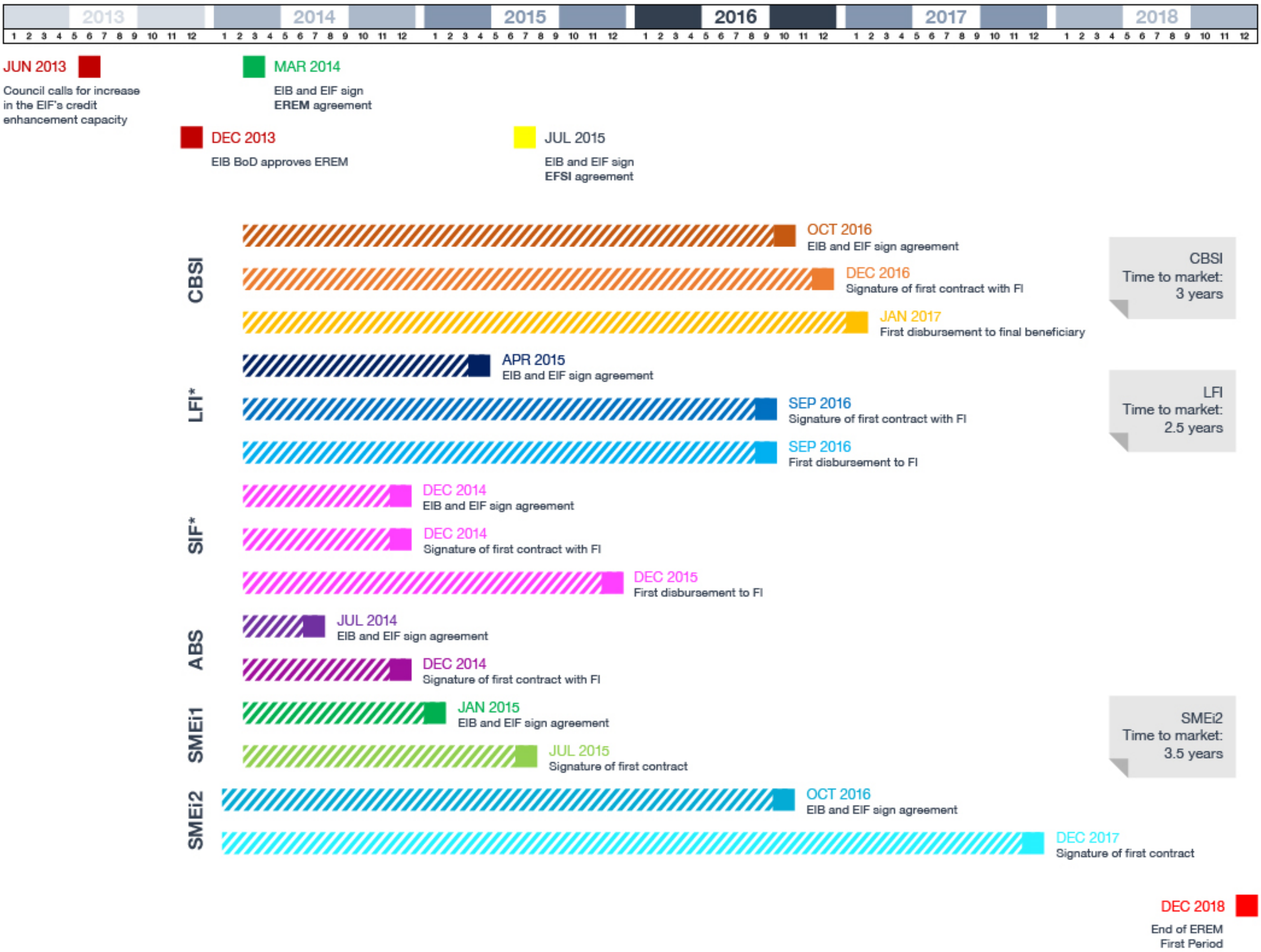
[26] Unlike other EREM instruments, the SME Initiative could not be directly applied by banks. A government or regional mandate to the EIF was required to implement this instrument.

[27] The SME Initiative has a layered structure: ESIFs cover the junior/lower mezzanine tranches, EU funds (COSME and Horizon 2020) cover the middle mezzanine tranches, while EIB Group resources are used for the upper mezzanine (EREM contribution) and, where relevant, the senior tranche (EIB).

– was challenging to implement as the EIF's systems were not geared up for loans to financial intermediaries in line with EIB loan standards.

Consequently, several EREM products took a relatively long time to develop and deploy (Figure 9). For example, following the launch of EREM, it took over 2.5 years for the CBSI Instrument agreement between the EIB and the EIF to be signed, almost three years for the first disbursement to SMEs to be made, and 3.5 years for the first contract under the SME Initiative Option 2 to be signed.

Figure 9. Time to market for EREM products



Source: EV

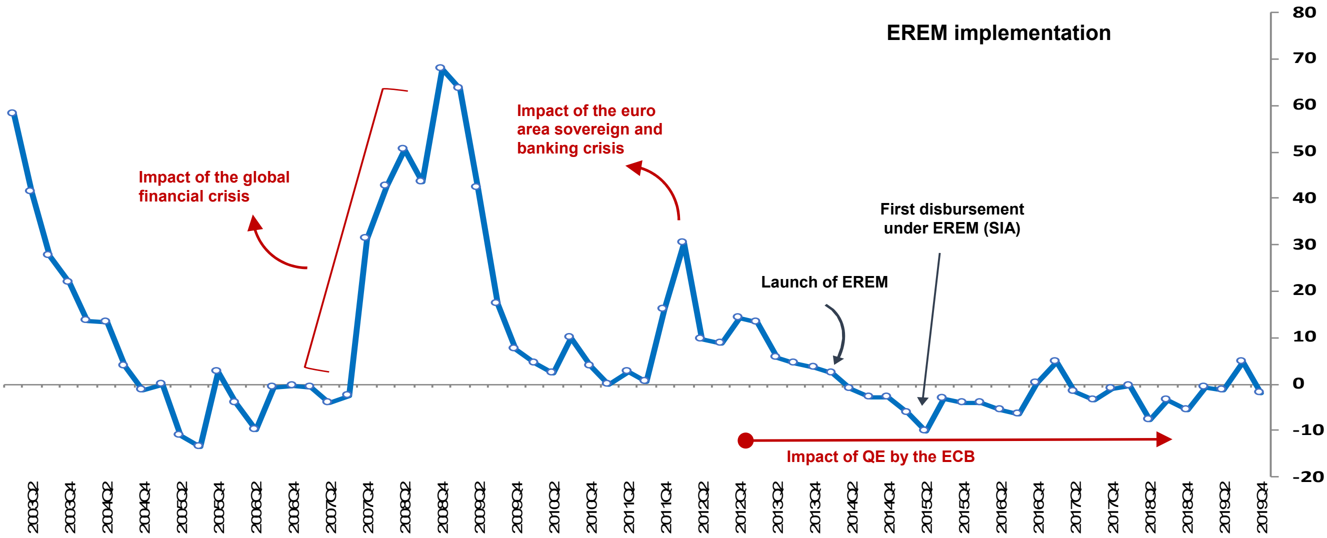
3.3 Limited relevance of EREM in addressing cyclical gaps in SME financing due to overall improvement in financing conditions

Despite the urgency expressed by the European Council, it took a relatively long time for EREM financing to reach the market. By the time EREM was launched, financing conditions for businesses had already started improving (primarily due to the accommodative monetary policy of the ECB). Moreover, by the time EREM products reached the market, the cyclical issues in the availability of finance had practically disappeared in most MS, although financing gaps persisted in some MS such as Spain, Greece, Italy, Latvia and Cyprus (see section 3.4).

Figure 10 depicts the quarterly change in credit standards on loans to enterprises[28] applied by euro area banks between Q1 2003 and Q4 2019. It shows that euro area banks significantly tightened their credit standards on loans to enterprises from Q3 2007 onwards. The intense net tightening of credit standards during this period reflects the deterioration in the economic outlook and creditworthiness of borrowers, as well as banks' adjustment of their risk attitude. The net tightening of credit standards peaked in Q3 2008 following the September collapse of the investment bank Lehman Brothers. After a temporary improvement in financing conditions in the euro area, the emergence of tensions in the sovereign bond markets of some euro area countries in the second half of 2011 changed the situation again. There was a second, albeit smaller, peak in the net tightening of credit standards in Q4 2011, raising intense concerns about a shortage of liquidity in the banking system, especially in the euro area countries hit hardest by the crisis.

A series of monetary policy measures by the ECB (e.g. interest rate cuts and quantitative easing), together with banks' balance sheet repair and the gradual recovery of the euro area economy, contributed to a net easing of credit standards from Q4 2012 onwards.

Figure 10. Euro area banks' credit standards on loans to enterprises (net percentage*)



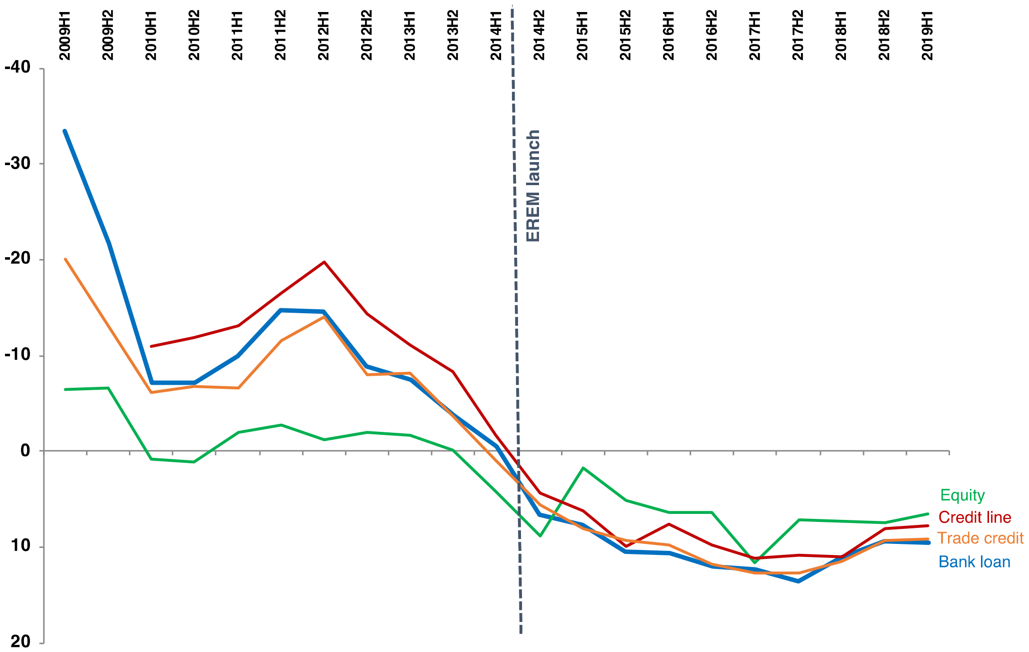
* *The net percentage is the difference between the sum of the percentages of banks responding "tightened considerably" and "tightened somewhat" and the sum of the percentages of banks responding "eased somewhat" and "eased considerably".*

Source: The euro area bank lending survey, ECB Occasional Paper Series, September 2016

[28] According to the glossary of the ECB's euro area bank lending survey, "Credit standards are the internal guidelines or loan approval criteria of a bank. They are established prior to the actual loan negotiation on the terms and conditions and the actual loan approval/rejection decision."

The results of the ECB SAFE survey corroborate the above trend. Figure 11 shows that the availability of bank loans, credit lines (including bank and credit card overdrafts), trade credit and equity financing had gradually started recovering in 2012 and that this trend continued through most of the EREM implementation period (2014-2018).

Figure 11. Change in the availability of external financing for euro area SMEs (net percentage*)



* *The net percentage is the difference between the percentage of firms reporting an improvement in the availability of external financing and that reporting a deterioration. Positive (negative) values indicate that the proportion of firms reporting an improvement in the availability of external financing is higher (lower) than the proportion reporting a deterioration.*

Source: ECB SAFE survey

Moreover, the joint Commission-ECB SAFE survey[29] results indicate that the importance of access to finance for EU SMEs steadily declined from 2013 to 2018, both relative to other issues constraining SMEs and in absolute terms. In 2013, access to finance was the most pressing problem for 15% of EU SME managers,[30] behind only finding customers. Yet by 2018 this percentage had declined to 7% and access to finance was the least cited by survey respondents as the most pressing problem, with other problematic issues – the availability of skilled staff, finding customers, competition, regulation and the costs of production or labour – all relatively increasing in importance. These results are corroborated by the EIBIS, in which 11% of participating firms stated that "availability of finance" is a major obstacle[31] and 5% reported facing external finance constraints (4% of large firms and 6% of SMEs).[32] Although perceptions around the availability of finance considerably improved during EREM implementation, these were still well below pre-crisis levels.

[29] The ECB SAFE survey covers euro area countries only, whereas the joint Commission-ECB SAFE survey covers the entire EU.

[30] In 2009 access to finance was **the most** pressing problem for 17% of EU SME managers

[31] This survey covers both small businesses and larger corporates. Available at: https://www.eib.org/en/publications/eibis.htm

[32] Finance-constrained firms include: those dissatisfied with the amount of finance obtained (received less); firms that sought external finance but did not receive it (rejected); and those that did not seek external finance because they thought borrowing costs would be too high (too expensive) or that they would be turned down (discouraged).

3.4 EREM was nevertheless highly relevant in addressing structural issues in access to finance for SMEs, small mid-caps and social enterprises and tackling bank financing gaps in some MS

Despite the overall improvement in financing conditions, EREM was still highly relevant due to continuing market gaps and deficiencies in access to finance for SMEs and small mid-caps. Most notably:

Structural gaps in access to finance for certain types of businesses and for certain types of investment needs: While the cyclical issues in finance availability waned during 2014-2018, endemic problems remained for certain types of firms such as social enterprises and companies with specific business models or needs. For example, a considerable body of literature suggests that social enterprises face particular challenges in accessing repayable finance: they are less likely to have the collateral of individual entrepreneurs and can appear less attractive to lenders and investors as they have to balance their social mission with commercial objectives.[33]

Furthermore, research undertaken as part of this evaluation shows that loan funds address the financing needs of businesses that are not well served by banks. For example, loan funds offer financing for certain types of projects which are often refused by banks (e.g. event-driven transactions, hiring of personnel, overseas expansion, etc.) or offer financing more suited to the needs of certain businesses in terms of tenor (longer tenor compared to banks), flexibility (e.g. bullet repayment structure), or speed (loan funds take two to three weeks to approve a loan, whereas banks can take months to approve business loans).

Underdeveloped markets for non-bank sources of finance: European SMEs have historically been heavily reliant on banks for their external financing needs, receiving more than 75% of their external finance from banks.[34] This over-reliance on banks put them under pressure during the global financial crisis of 2008-2009 and the subsequent sovereign debt crisis in Europe. The paralysis of the interbank lending market (which is a main source of liquidity for credit institutions) and the collapse of major wholesale markets (like securitisation) resulted in a significant tightening of credit conditions in 2008-2009. The resulting balance sheet consolidation and deleveraging imposed by the newly approved prudential regulations further added to the credit crunch. Due to structural reasons[35] and their higher vulnerability to economic downturns,[36] the credit crunch ended up hitting SMEs harder than larger firms.[37] Even though bank lending to NFCs has recovered since late 2014, net credit flows remained rather low throughout the EREM implementation period, particularly in the euro area.

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33 Lyon, F. and Owen, R., Financing social enterprises and the demand for social investment, 2019.

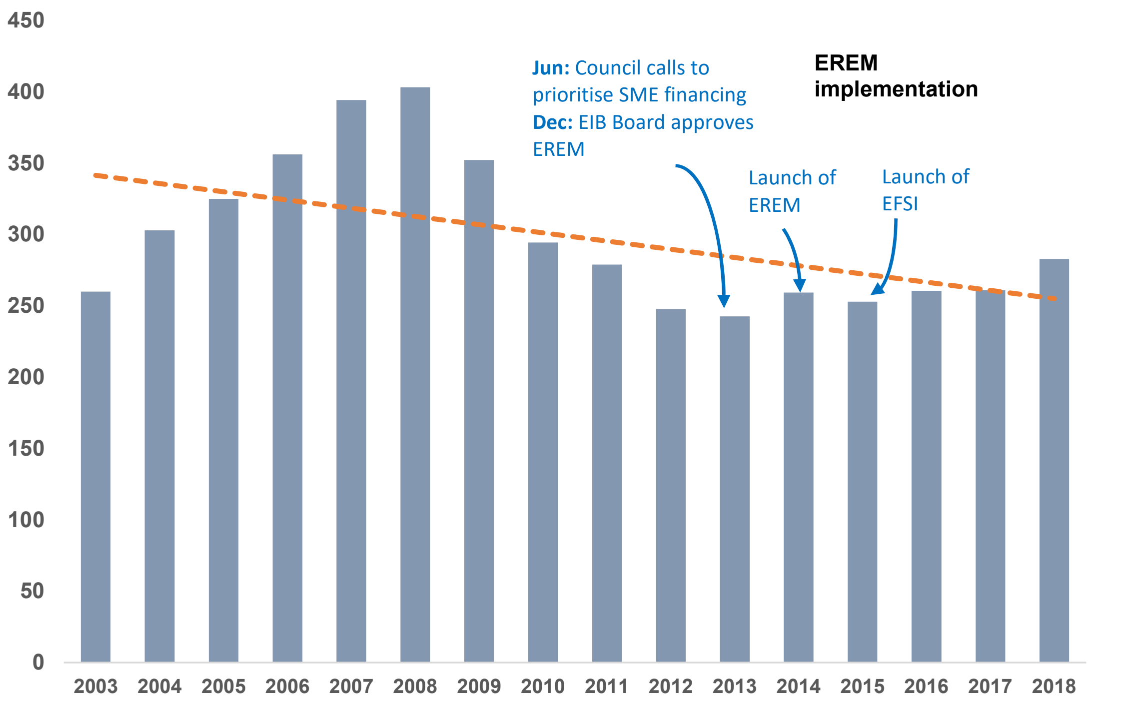
34 COM (2015) 468 final – Action Plan on Building a Capital Markets Union.

35 SMEs are more opaque and their corporate capabilities more difficult to assess than larger firms, because their financial statements are less informative and their credit histories are usually shorter. These characteristics are compounded by fixed costs in external assessment and monitoring. All this leads to SMEs facing higher transaction costs, especially those stemming from asymmetric information.

36 SAFE survey data show that SMEs' profits, liquidity buffers and own capital have developed less favourably compared to those of large firms during the crisis.

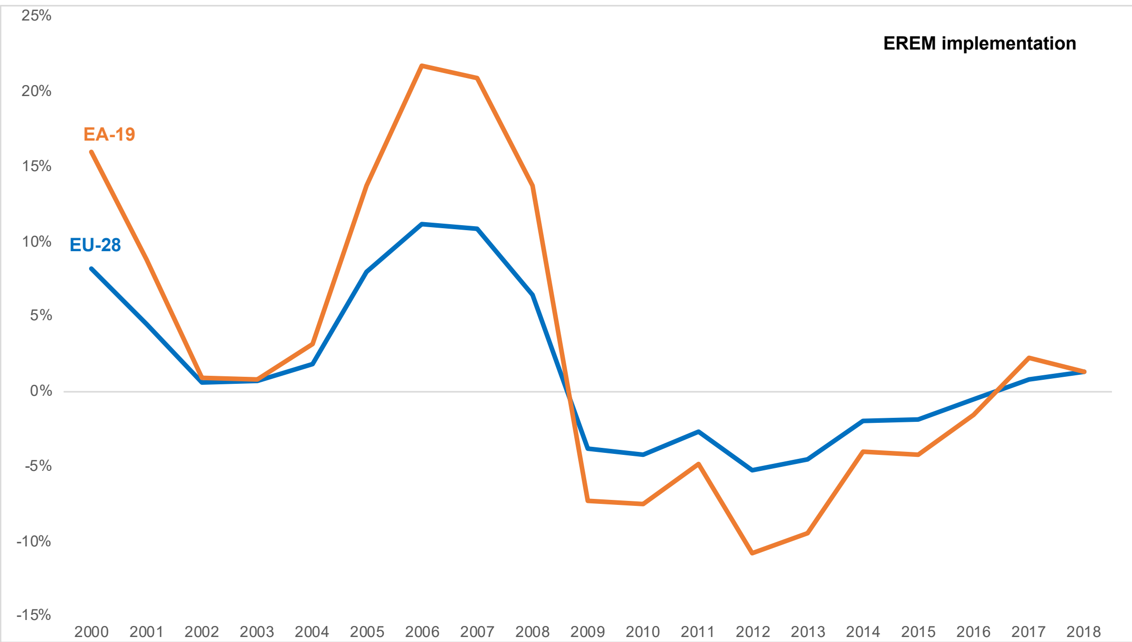
37 In addition to the general tightening of credit standards, the spread between borrowing costs of SMEs and those of large enterprises widened significantly during the crisis. See DB Research, SME financing in the euro area: New solutions to an old problem, 2014.

Figure 12. Lending to NFCs in the euro area, 2003-18 (€ bn)



Source: ECB
Credit and other institutions (MFI except monetary market funds and central banks) – Loans (new business) other than revolving loans and overdrafts, convenience and extended credit card debt.

Figure 13. Year-on-year percentage change in credit to NFCs, EU and euro area, 2000-2018



Source: European Credit Research Institute Statistical Package

In the above context, it was a highly relevant medium to long-term objective to diversify the sources of financing available to SMEs and small mid-caps, especially since some of these alternative channels of finance were underdeveloped at the time (see Box 4). Moreover, this EREM objective was aligned with the Commission's Action Plan on a Capital Markets Union published in September 2015 which, among other aims, sought to broaden the range of financing options available to businesses.

Box 4. Underdeveloped non-bank sources of finance: the case for the SIA, the LFI and the CBSI Instrument

SIA

A study by the Commission shows that the EU impact investment market was broadly classified as "emergent" in 2014.[38] There were very few social impact funds established in the European Union, while there was high and increasing demand for finance from social enterprises. A range of other sources also conclude that access to finance was a challenge for social enterprises.

A 2018 Joint Research Centre study[39] reported growth in the social investment market since 2014 but concluded that much more development is needed at the pan-European level. 16 MS were still classified as "1" (low maturity), while seven MS were classified as "2" (medium maturity) and five as "3" (high maturity), namely the United Kingdom, Italy, France, Germany and Belgium. It is therefore clear that much more needs to be done to achieve a sustainable social investment market at the pan-European level.

The literature also underlines the important role of the public sector in establishing and growing impact investment markets. In many countries, public authorities alone are unable to effectively address the scale and range of social issues, such as provision of childcare, rehabilitation of ex-offenders and provision of social care or housing. Social enterprises can therefore make an important contribution in these domains. The United Kingdom's experience demonstrates the important enabling role of the public sector in establishing and growing the impact investment market.

LFI

At the time of conceptualisation of EREM, private debt markets were in infancy or non-existent. Only a minority of existing debt funds focused on SMEs and small mid-caps, while the majority were targeting bigger mid-caps to large caps. The asset class did not exist in most MS due to the lack of a legal framework or low investor appetite.

CBSI Instrument

Regional CBSI typically have a strong focus on SMEs, particularly on microenterprises and small SMEs, for which they are an important source of financing. The CBSI business model relies on features particularly well suited to these clients, as it is characterised by strong relationship banking, local embeddedness, relatively dense branch networks and a decentralised nature.

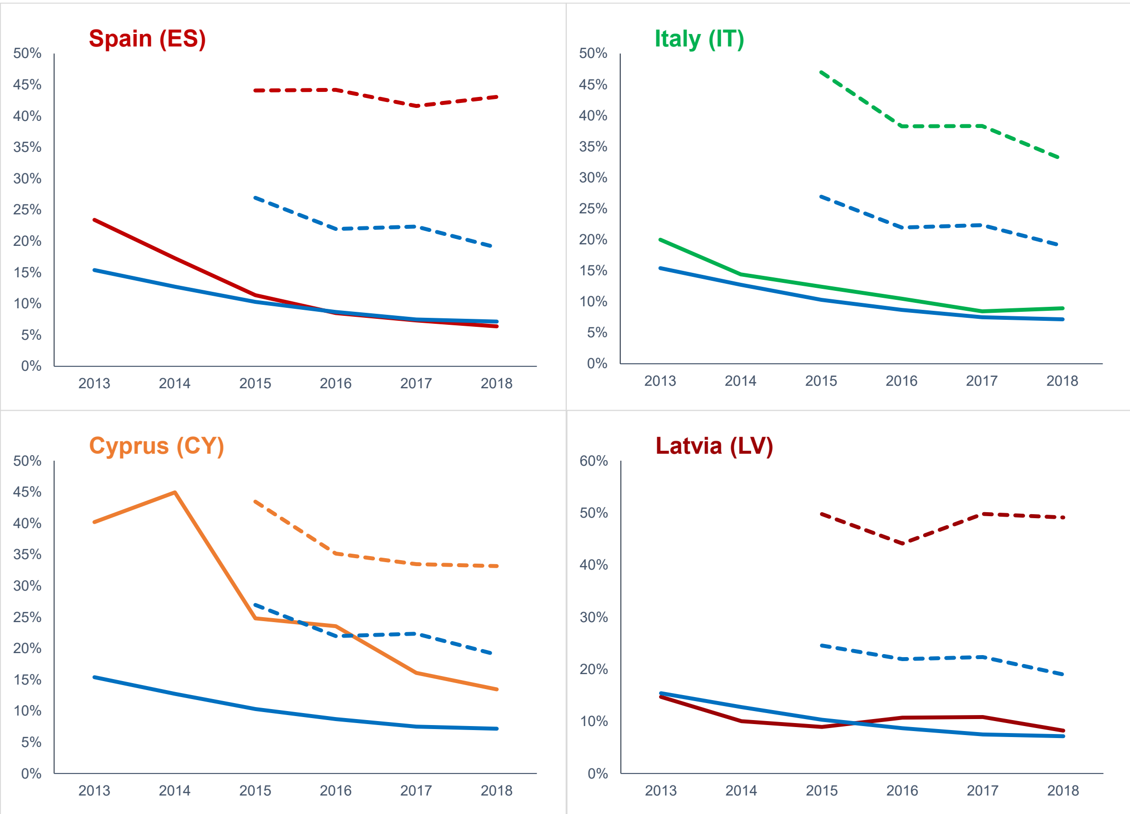
However, the capacity of regional CBSI to lend to SMEs is constrained by their funding model. The main funding sources for cooperative banks are deposits and retained profits. They have only limited access to external capital, unless they are part of a larger banking group. For instance, cooperative banks cannot raise large amounts of capital quickly by issuing shares on a stock market. It is difficult for them to issue equity (shares) to outside investors because they are owned by their members (typically depositors and savers) and issuing equity would dilute their cooperative ownership. Similarly, for small banks, retail deposits account for a considerably larger share of overall funding than wholesale sources, while the lending capacity of leasing companies is often constrained by their small equity base. By providing senior unsecured loans to CBSI, EREM sought to diversify their sources of funding (particularly long-term funding), thus enhancing their capacity to lend to SMEs.

38 European Commission, A map of social enterprises and their eco-systems in Europe, 2015.

39 Joint Research Centre, Social Impact Investment in the EU. Financing strategies and outcome-oriented approaches for social policy innovation: narratives, experiences and recommendations, 2018.

Persistent bank financing gaps in some MS: Although financing conditions eased markedly from 2014 (coinciding with the launch of EREM), major constraints persisted in some MS throughout the EREM implementation period. For example, according to ECB SAFE survey data, while 85% of German SMEs and 72-79% of Austrian, Finnish and French SMEs were granted the full amount of credit they requested during October 2012 to March 2013, the ratio was much smaller in Greece (25%), Italy (57%), Ireland (32%), the Netherlands (46%), Portugal (55%) and Spain (40%). The ECB also calculates an indicator called "financing obstacles for SMEs", which is the sum of the percentages of SMEs reporting loan applications that were rejected, granted only a limited amount, or dropped by the SME because the borrowing cost was too high, and the percentage of SMEs that did not apply for a loan for fear of rejection. The share of SMEs reporting such financial obstacles ranged between 51% and 64% in Greece, Ireland and Spain and between 31% and 46% in Portugal, Italy and the Netherlands. By contrast, the share of financially constrained SMEs was 9% in Germany, 14% in Austria and 18% in Finland. In Spain, Italy, Latvia and Cyprus over one-third of firms reported availability of finance as a major obstacle throughout the EREM implementation period (Figure 14).

Figure 14. MS with the most pressing financing needs as perceived by SMEs and corporates

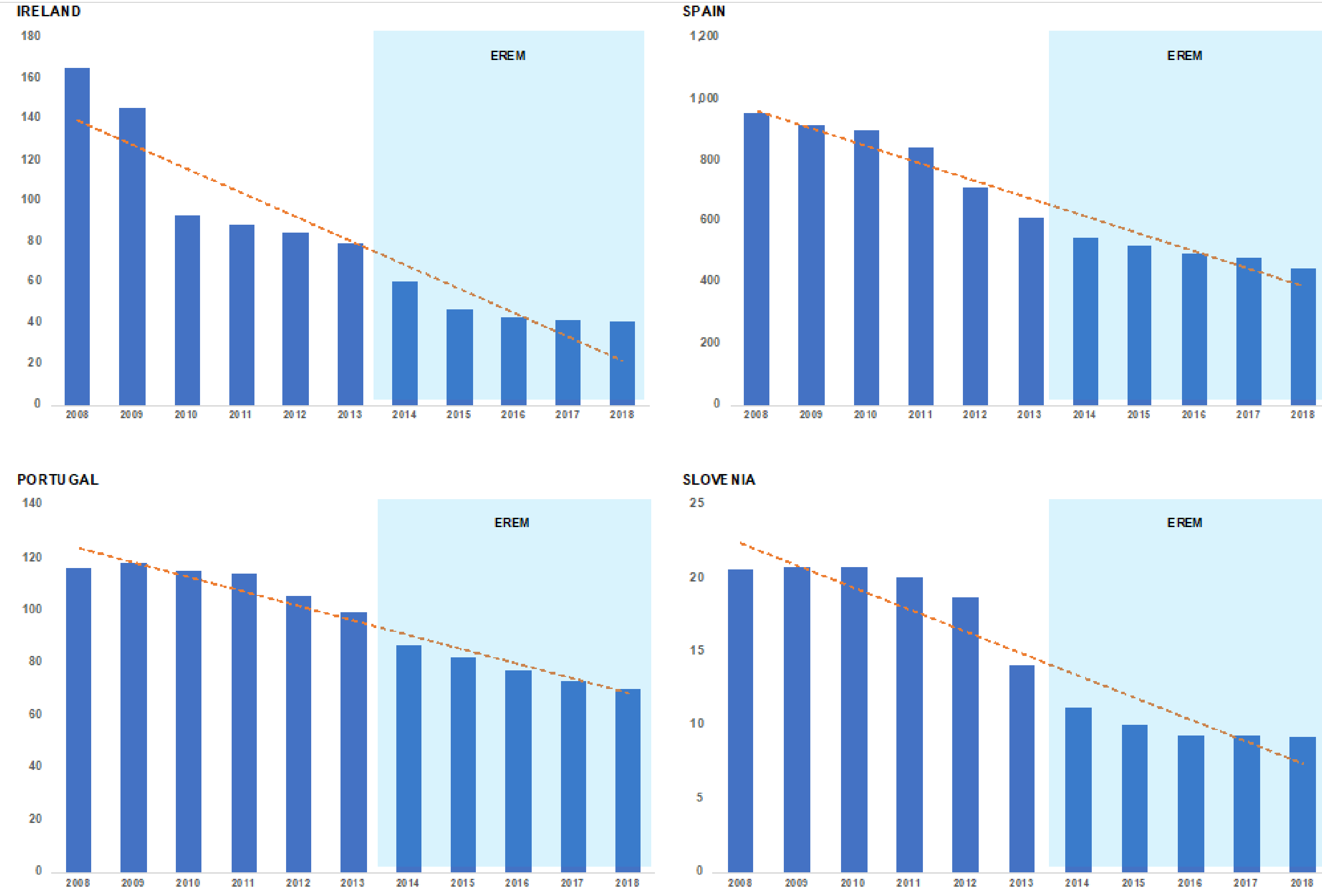


ECB SAFE: % of firms stating "access to finance" is currently the most pressing problem they face.
EIBIS: % of firms stating that "availability of finance" is a major obstacle.
N.B. Greece is excluded as there were special initiatives in place as part of the economic adjustment programmes.

Sources: ECB SAFE survey and EIBIS

Similarly, bank lending to NFCs continued to decline throughout the EREM implementation period in several MS, remaining far below pre-crisis levels in Ireland, Spain and Slovenia (Figure 15).

Figure 15. Bank lending to NFCs in selected MS, 2008-2018 (outstanding value, € bn)

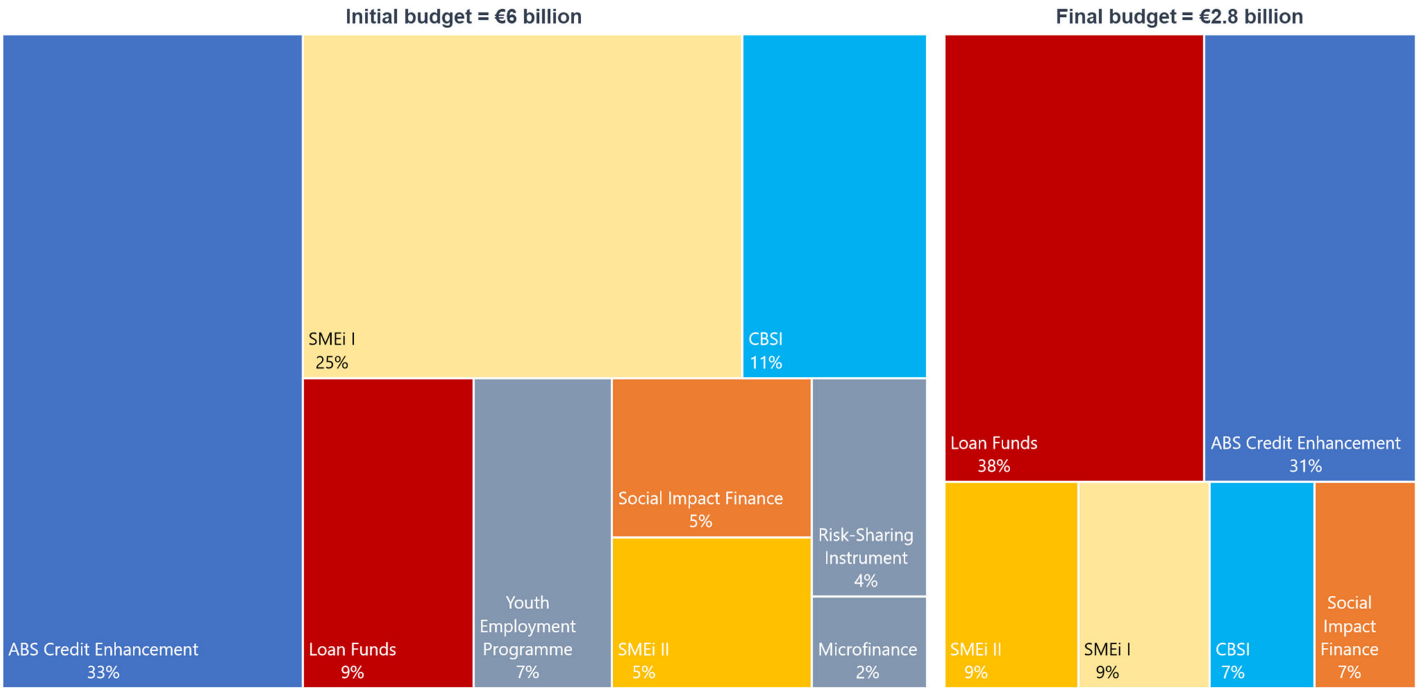


Source: European Credit Research Institute Statistical Package

3.5 Strong take-up of some EREM products further illustrates their market relevance

There was particularly strong market demand for the LFI. An initial sum of €175 million was earmarked for the LFI for the first period of EREM implementation. This was first increased to €725 million (€550 million reallocated from the SME Initiative Options 1 and 2) and finally to €1 052.8 million (€327.8 million reallocated from the SME Initiative Option 1 and ABS Credit Enhancement) due to the strong market demand. The share of the LFI thus increased considerably both in absolute and relative terms within the EREM financial envelope (Figure 16).

Figure 16. EREM budget allocation

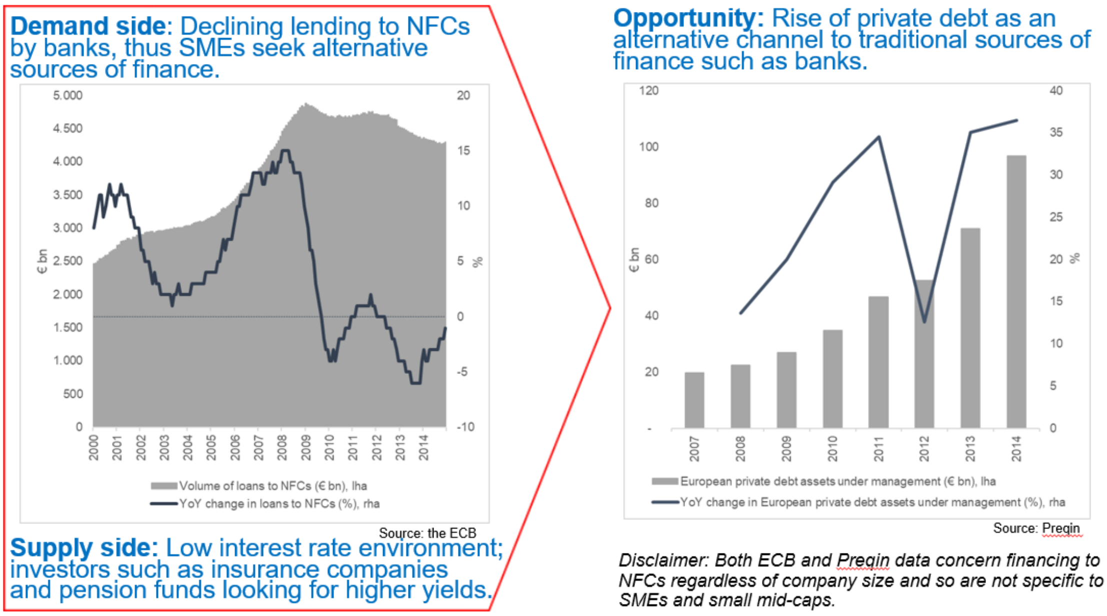


Source: EV based on data sourced from the EREM final report (EIF)

The strong demand for the LFI not only reflects broader market conditions, which were highly favourable for development of the private debt industry (Figure 17), but also the effective design and positioning of the product:

- The product focused on the lower mid-market segment (fund size < €1 billion) where EIF investment was most needed;
- It supported both selective and diversified loan funds;
- Preference was given to funds whose core lending strategy and/or competence was already oriented towards the SME and small mid-cap segment, rather than imposing upon funds to change their strategy;
- The intensive due diligence process was highly valued by fund managers and other investors;
- The product included support for many first-time teams and first closings, in line with its market development objective;
- Structuring and legal support was provided to first-time teams and to niche and/or complex transactions (e.g. P2P, asset-backed financing).

Figure 17. Market context and opportunity for the LFI



Disclaimer: Both ECB and Preqin data concern financing to NFCs regardless of company size and so are not specific to SMEs and small mid-caps.

Moreover, there has been strong take-up of products such as the SIA and ABS Credit Enhancement (Table 3). The €189 million budget for the SIA has been fully absorbed.[40] The SIA shared many design features with the LFI, such as clear market positioning, support for first-time teams, provision of structuring input and rigorous due diligence, as well as additional features such as an impact-based carry methodology and a social impact measurement methodology which added to its attractiveness (these are further discussed in section 5).

The ABS Credit Enhancement product allowed the EIF to finance securitisation transactions that it would not have been able to undertake with its own resources. Specifically, it allowed the EIF to achieve a scalable effect in the SME securitisation market, in terms of larger ticket size and broader scope.[41] This enabled the EIF to provide capital relief[42] to originators, thus incentivising them to provide new financing to SMEs and mid-caps, in a market context characterised by regulatory developments and pressure on banks' capital structure.

40 The SIA was an existing product, initially piloted in 2011 in response to the growing demand for equity finance to support social enterprises. The EREM budget was used to top up and extend the SIA.

41 From AAA (senior) to BB (mezzanine).

42 By guaranteeing the securitised portfolios.

Table 3. Take-up of EREM budget

	Initial Budget Allocation € m			Final Budget Allocation € m	Commitment as of 31 Dec 2019 € m	Signatures as of 31 Dec 2019 € m	Budget Utilisation	
	First Period (2014-16)	Second Period (2016-18)	Total				Commitment as % of Final Budget	Signatures as % of Final Budget
EREM products that were rolled out								
ABS Credit Enhancement	890	1 060	1 950	855	855	855	100%	100%
SME Initiative Option 1	1 310	490	1 500	245	280	266	114%	108%
SME Initiative Option 2			300	250	19	19	8%	8%
Loan Funds Instrument	175	350	525	1 053	868	781	82%	74%
Social Impact Finance	189	126	315	189	189	176	100%	93%
CBSI Instrument	280	350	630	195	153	152	78%	78%
Subtotal	**2 844**	**2 376**	**5 220**	**2 787**	**2 364**	**2 248**	**85%**	**81%**
EREM products that were dropped								
Youth Employment Programme	300	125	425					
Microfinance Instrument	53	52	105					
Risk-Sharing Instrument	200	50	250					
Subtotal	**553**	**227**	**780**					
Total: EREM	**3 397**	**2 603**	**6 000**					

Note: Commitment data report initial commitments

Source: EV based on data sourced from the EREM final report (EIF)

By contrast, the SME Initiative was slow to take off due to its complex capital structure, the formal processes required for managing authorities to sign up to this programme (which slowed down origination and development) and the wait-and-see approach adopted by several managing authorities.

Despite being highly relevant, market interest in the CBSI Instrument was lower than expected and this was ultimately reflected in the products' budget being reduced from €280 million to €195 million, and in a relatively low absorption rate compared to other EREM products such as the LFI and the SIA (only 80% of the budget, or €153 million, was committed). The following factors constrained the take-up of the instrument:

- *Eligibility criteria:* Although driven by risk considerations, general eligibility imposed some constraints on the financial intermediaries, such as (a) minimum credit risk rating assigned by the EIB Group to the financial intermediary; (b) exclusion of financial intermediaries already benefiting from Loans for SMEs (L4SME);[43] and (c) specific risk-related issues raised by the EIB and relating to certain types of potential financial intermediaries (e.g. German leasing entities).
- *Timing of marketing*: The long delay (around 2.5 years) before the CBSI Agreement between the EIB and the EIF was signed adversely affected the marketing of the CBSI Instrument, as it created uncertainty over the timing of approval and implementation of the instrument.

[43] L4SME is the core EIB product supporting SMEs' access to finance.

3.6 Recap of key messages

- EREM was approved by the BoD in December 2013 against the backdrop of a fragile and uncertain economic recovery, declining levels of bank lending and high levels of youth unemployment.
- Although EREM was conceived alongside an increase in the EIF's capital base to boost the EIF's overall risk-bearing capacity, it was designed as a mandate with its own specific objectives.
- The first and second objectives of EREM (to enhance access to finance for social enterprises, SMEs and small mid-caps, and to contribute to the development of capital markets) were highly pertinent. However, the third objective (see Box 3) was too ambitious, far-ranging and vague. It sought to address a number of issues such as microfinance, youth unemployment and innovation.
- Overall, EREM objectives were not articulated in precise terms, which somewhat undermined the usefulness of goal setting.
- The choice of products within the Mandate was not well suited to its (implicit) objective of quickly getting money flowing into the real economy. Its design was overly complex, consisting of several different types of products (equity, unsecured senior loans, different types of securitisation products) and targeting different types of intermediaries (impact funds, private debt funds, CBSI, etc.) and final beneficiaries (social enterprises, SMEs, small mid-caps). Some products were new and untested (e.g. LFI) while some other products were inherently complex (e.g. SME Initiative). Several EREM products took a relatively long time to develop and reach the market. Consequently, by the time EREM was up and running, financing conditions for businesses had considerably improved in most MS.
- Nevertheless, some EREM products were still highly relevant given the structural issues in access to finance for SMEs, social enterprises and small mid-caps, the bank financing gaps in some MS and the underdeveloped nature of alternative sources of finance. Also, EREM was well designed (in terms of the final product choice) to address these issues.
- The strong take-up of some EREM products further illustrates their relevance. There was very strong market demand for the LFI. In response to the high level of market interest for this product, its budget was increased by a factor of six. There was also strong take-up of products such as the SIA and ABS Credit Enhancement. The budget allocated to these products has been fully absorbed. By contrast, demand for the CBSI Instrument and the SME Initiative fell short of expectations for various reasons, including design complexity, slow implementation and marketing constraints.

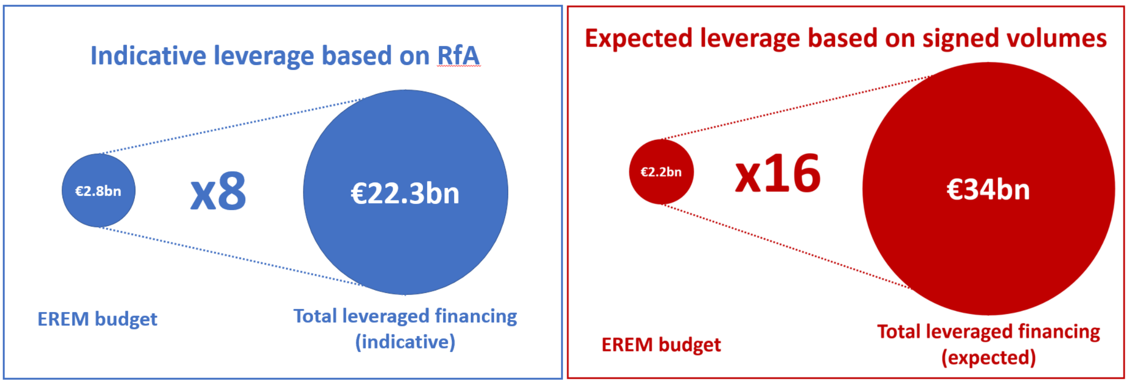
4. Effectiveness in Enhancing Access to Finance for SMEs, Small Mid-Caps and Social Enterprises

This section assesses the extent to which EREM has achieved its primary objective of enhancing access to finance for SMEs, small mid-caps and social enterprises. It first considers the total financing that is likely to be leveraged by the Mandate over its lifetime. The section then examines the extent to which this financing would have materialised even without EREM support, and takes stock of the volume of financing that has actually reached the real economy until mid-2019. Finally, it examines the geographical distribution of EREM financing in relation to access-to-finance gaps reported by SMEs and corporates in different MS.

4.1 EREM has increased the availability of finance for SMEs, small mid-caps and social enterprises

The total financing expected to be leveraged by EREM has exceeded expectations. €1 from EREM is expected to leverage €16 of financing for SMEs, small mid-caps and social enterprises. This exceeds the indicative leverage of x8 anticipated at the time EREM was approved. By the end of 2019, the EIF had signed deals amounting to €2.2 billion with financial intermediaries located in 21 MS. This contribution from EREM is expected to leverage almost €34 billion of financing for SMEs, small mid-caps and social enterprises over a ten-year period (2014-2023), which is 1.5 times higher than the target volume of €22.3 billion.[44]

Figure 18. Indicative versus expected leverage of EREM as of 31 December 2018



Figures for EREM budget and indicative leverage based on EREM Request for Approval (RfA).
Indicative leveraged financing is calculated as EREM budget for each product for the first period x indicative leverage. See Annex 4 for calculations.
Expected leveraged financing based on signed volumes. Leverage is calculated as total leveraged financing divided by EREM signatures.

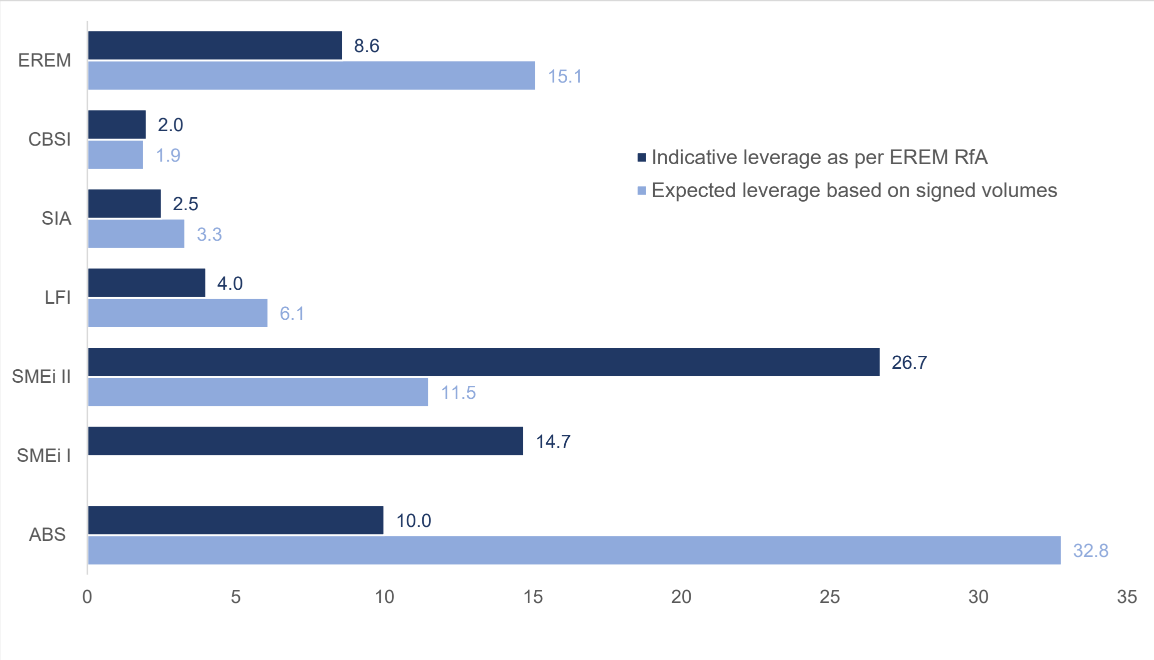
Source: EV based on data from the EREM final report (EIF)

However, the data on financing leveraged by EREM needs to be interpreted with some caution. There is insufficient evidence to conclude that this entire volume of financing leveraged is additional. It is possible that part of this financing would have been made available by the market to SMEs and small mid-caps even in the absence of EREM (see section 4.2 for further discussion on this topic).

[44] Target volume for first period calculated as follows = EREM budget x indicative leverage for each product. See Annex 3 for calculations

With the above caveat in mind, the analysis below compares between indicative leverage (based on EREM RfA) and expected leverage (based on signed volumes). This provides a basis for comparing actual performance versus planned performance.

Figure 19. Indicative versus expected leverage of EREM products



Financing expected to be leveraged by the SME Initiative Option 1 is not available.

Source: EV based on data from EREM final report (EIF)

The ABS Credit Enhancement product has been particularly successful in leveraging financing for SMEs and small mid-caps. By the end of 2018, the EIF had closed transactions amounting to €851 million with six counterparties in five MS (Italy, Germany, Poland, Austria and the United Kingdom). Based on signed volumes, the product is expected to make available almost €28 billion of capital for financing SMEs and small mid-caps. This corresponds to an extraordinarily high leverage of x33. Leverage based on contractually committed amounts is considerably lower (x6). Based on the EIF's experience with products of this nature, actual leverage is expected to be closer to the target (x10).

The leverage effect of the LFI and the SIA has also exceeded expectations. During the 2015-2018 period, the LFI invested €761 million in 20 loan funds located in six MS.[45] This investment is expected to mobilise €4.8 billion of capital, a significant proportion of which is expected to be used for financing SMEs and small mid-caps.[46] The expected leverage of x6.1 exceeds the planned leverage (x4).

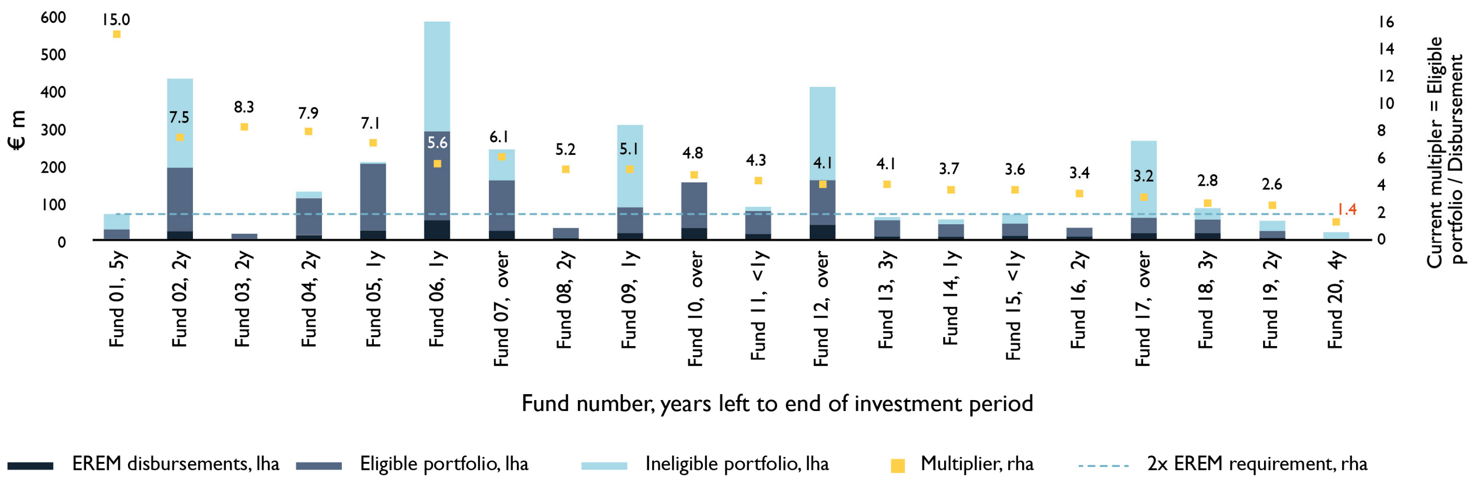
EREM-backed loan funds have already lent more than the minimum required by EREM to SMEs and small mid-caps. Under the LFI, fund managers were obliged to invest an amount equal to at least double the overall amount disbursed from EREM into eligible beneficiaries (SMEs and small mid-caps). As of 30 June 2019, 19 (out of 20) loan funds were already lending more

[45] Germany, France, Italy, the Netherlands, Spain and the United Kingdom. It should, however, be noted that seven of the supported loan funds have a multi-country strategy, which means that the actual geographical reach of the product will be wider.

[46] Mid-caps (500 ≤ employees < 3 000) account for 12% of LFI final beneficiaries and 36% of the funding. Although ineligible under EREM, they fall within the remit of support from the EIB Group. Also ineligible under EREM, large-caps account for the smallest proportion of beneficiaries (2%) and financed amounts (8%).

than twice the amounts disbursed by EREM to their funds. Only one fund was lending less than the requirement (x1.4), but is still four years from the end of its investment period (see Figure 20).

Figure 20. Fund-level multiple: Investment in SMEs and small mid-caps as a multiple of EREM disbursements



Source: Based on data provided by the EIF

Under the SIA, the EIF has invested €148 million in 14 impact funds located in eight MS.[47] These funds were expected to invest at least double the SIA investment amount into social enterprises. At the end of 2018, the total capital made available by the SIA-backed funds was €580 million, which is approximately four times higher than the amount invested by the SIA.

The leverage effect of the CBSI Instrument is in line with expectations. The CBSI Instrument was taken up by 15 financial intermediaries[48] in eight MS.[49] This product took the form of small senior, typically unsecured loans to lower-rated financial intermediaries for on-lending to SMEs and small mid-caps. For this product, the signed volume of €143 million is expected to mobilise €284.5 million of financing (x2) for microenterprises and SMEs (though no mid-caps have been financed).

The leverage effect of the SME Initiative, by contrast, has fallen short of expectations. The SME Initiative is expected to mobilise €4.5 billion of SME financing in six MS.[50] While the budget for Option 1 (see Box 5 for explanations of the two options) was almost fully absorbed, Option 2 was only used in Italy with a rather small EREM participation (€19.3 million). Based on current estimates, EREM financing has contributed to creating an additional portfolio of SME loans amounting to €223 million, which represents an expected leverage of x11.5 (these should be regarded as preliminary estimates that are subject to change, as the inclusion period is still open). It is understood that the ability of counterparties to originate loans under the SME Initiative Option 2 was significantly delayed in Italy by the implementation of the National State Aid Register. Originators faced a number of technical problems when the register was first introduced. To support the SME Initiative in Italy during this difficult initial phase, the EIF contributed its own resources to the implementation of solutions to facilitate use of the register.

47 Germany, Denmark, the United Kingdom, France, the Netherlands, Italy, Hungary and Spain.
48 One contract was cancelled.
49 Austria, Estonia, Germany, Italy, Lithuania, Malta, Romania and Sweden.
50 Spain, Malta, Bulgaria, Romania, Finland and Italy.

Box 5. Overview of the SME Initiative

The SME Initiative Option 1 is a joint guarantee (EU funds and European Structural and Investment Funds (ESIF)) combining multiple resources at different seniority levels. Its ultimate goal is to provide uncapped portfolio guarantees and partial capital relief to financial intermediaries building up new portfolios of debt finance instruments for and guarantees to SMEs and small mid-caps. The SME Initiative has a layered structure: ESIFs cover the junior/lower mezzanine tranches, EU funds (COSME[51] and Horizon 2020) cover the middle mezzanine tranches, while EIB Group resources are used for the upper mezzanine (EREM contribution) and, where relevant, the senior tranche (EIB).

Under Option 2, financial intermediaries securitise existing portfolios of debt finance to SMEs and small mid-caps or new portfolios of debt finance to SMEs, aiming at regulatory capital relief and/or new funding sources. Option 2 also follows a layered capital structure similar to Option 1. However, whereas Option 1 adopts a country-wide portfolio approach, the EIF implements the Option 2 product on a deal-by-deal basis.

Counterparties are obliged to report, line by line, the portfolio originated under the SME Initiative. In addition, the SME Initiative imposes financial penalties on the originator where the required size of the additional portfolio is not achieved.

The EREM Instrument, under the SME Initiative Option 2, provides risk support for EIB senior exposure (outside EREM) and can also accommodate lower-rated transactions (on average Baa3) that are outside the EIB's standard risk appetite.

4.2 In the absence of EREM, much of the financing under the LFI, the SIA and the CBSI Instrument would not have materialised

The evaluation examined the extent to which the above-reported volumes of financing would have materialised even without EREM support through the LFI, the SIA and the CBSI Instrument. This involved an assessment of additionality. The concept of additionality reflects the basic idea that EIF financing (via EREM) should contribute beyond what is available from other sources. As such, the level of additionality reflects (a) the extent to which a financial intermediary would have been able to obtain the same volume of finance (as the EIF investment) from other sources (public or private) on similar terms and conditions and within the same timeframe; and/or (b) the extent to which EIF financing mobilised capital from other public or private sector entities that would not have otherwise invested in the financial intermediary.

There is strong evidence that much of the financing leveraged by the LFI would not have materialised in the absence of EREM support. Most of the fund managers who responded to the survey (11 out of 15) claimed that, without EREM support, their funds would have either not closed or not reached their target size.[52] Even with EREM support, most funds (16 out of 20) did not reach their target size. However, EREM support did help these funds to exceed their minimum size, enabling them to start operations.

The case studies provide further corroboratory evidence. For two (out of five) funds, there was clear-cut evidence that they would not have closed in the absence of EREM support, as these were first-time funds focusing on smaller ticket size transactions. In another case, the fund manager claimed that their fund would not have closed without EREM support and that this support had a material signalling effect for some institutional investors (pension funds and insurance companies). However, it was not possible to collect further evidence (e.g. by

[51] The EU programme for the Competitiveness of Enterprises and Small and Medium-sized Enterprises.
[52] Additionally, one fund would have taken longer to reach its target size and another fund would have been 14% smaller in size without support from EREM.

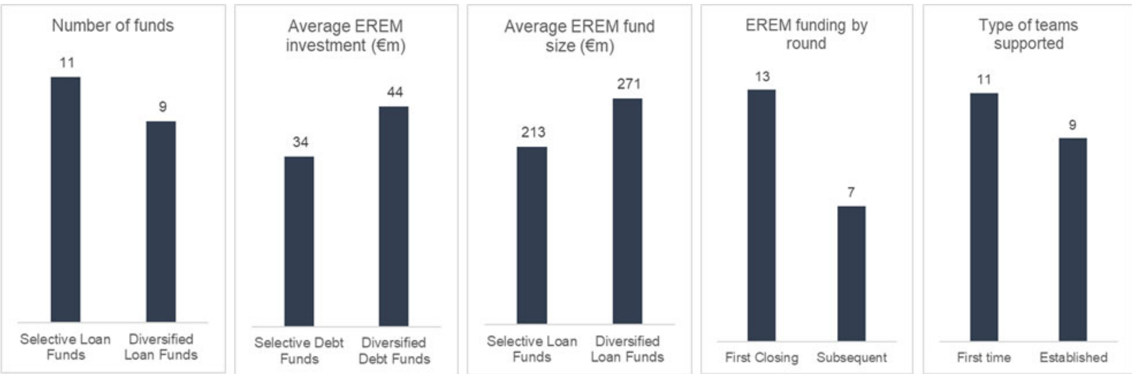
interviewing other investors in the fund) to validate this claim. In the other two cases, funds would have been smaller in size (below target but above minimum) in the absence of EREM support. Evidence suggests that the EIF played a strong catalytic role in attracting other investors to these two funds, one of which faced particular difficulty in fundraising due to its national market context.

An in-depth review of transaction documentation (such as due diligence reports) further shows that:

- LFI investment came in mainly at first closing, thus helping to catalyse other investors when most needed (see Figure 21);
- EREM support was particularly critical for those funds which struggled the most with fundraising. Seven (out of 20) funds did not achieve even 50% of their target size. These funds were mainly based in difficult market contexts or had specific assets (e.g. industrial leases, hybrid debt).

Moreover, interviews with fund managers revealed that EIF support was also instrumental in getting first-time funds off the ground. Indeed, EREM supported 11 first-time teams located in Italy, the United Kingdom, France, Spain, Germany and the Netherlands.

Figure 21. Characteristics of funds supported under the LFI

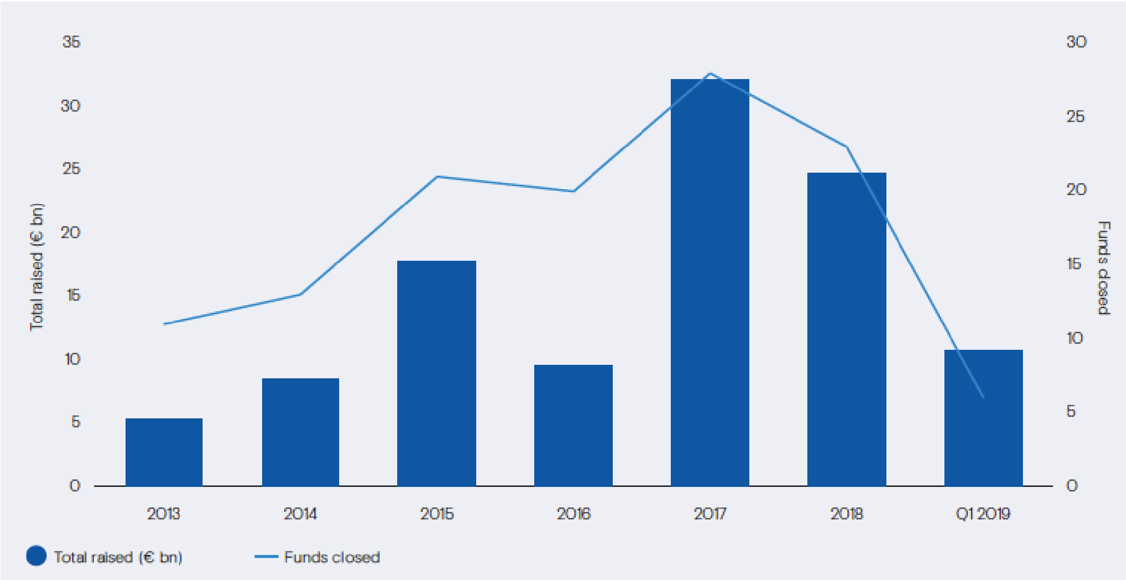


Source: EV analysis of EIF data

Arguably there is an element of bias in the views expressed by fund managers regarding the importance of EIF support. Nonetheless, wider evidence on the state of private debt markets strongly supports the fund managers' claims. In 2013-2014 there were very few debt funds active in the SME segment in Europe,[53] and hardly any institutional investors were putting money into this asset class due to its lack of a track record and doubts about its ability to meet their return expectations. These doubts were also echoed by fund managers interviewed in Italy, Spain and the Netherlands. Moreover, although direct lending has experienced huge growth over recent years (see Figure 22), there remains a strong preference among investors for established fund managers[54] and the lower mid-market segment (focusing on SMEs and small mid-caps) remains relatively small. According to a fund manager interviewed in the United Kingdom (where the private debt industry is more developed than in other EU countries), funds in this segment of the market would not have existed without public support (from the EIF and the British Business Bank).

[53] EIF, EIF Working Paper 2014/25 – Institutional non-bank lending and the role of debt funds, 2014.
[54] Preqin, Private debt spotlight, 2016. See also European Direct Lending Perspectives – Issue 2 Q1 2019 (Creditflux).

Figure 22. European direct lending fundraising



Source: European Direct Lending Perspectives – Issue 2 Q1 2019 (Creditflux)

Likewise, there is strong evidence that much of the financing made available to social enterprises by the SIA would not have materialised in the absence of EREM support. According to SIA-backed fund managers, without SIA investment, their funds would have either not closed (five out of 12 funds) or fallen short of their target size (seven out of 12 funds). None of the SIA-backed fund managers believed they would have been able to secure investment from alternative sources had the EIF not invested in their funds. When asked why their funds would not have closed or reached their target size, the fund managers indicated that no other public or private investors were willing to invest on the same scale as the EIF. These issues were further explored through in-depth case studies. In all five cases reviewed, the funds would have been much smaller in size without EIF investment. This is largely explained by the reluctance of larger institutional investors to invest in small-sized funds. The evaluation found examples where investors conditioned their commitments on the achievement of a minimum fund size (e.g. €30 million), which would have been difficult to reach without the substantial commitments made by the SIA (20-49.9% of the fund size). Some interviewed fund managers explained that they might have been able to secure part of the investment from other smaller investors in the absence of the EIF. However, in all cases this would have taken more time, thus delaying the start of the investment process, and would have also increased the fundraising costs.[55]

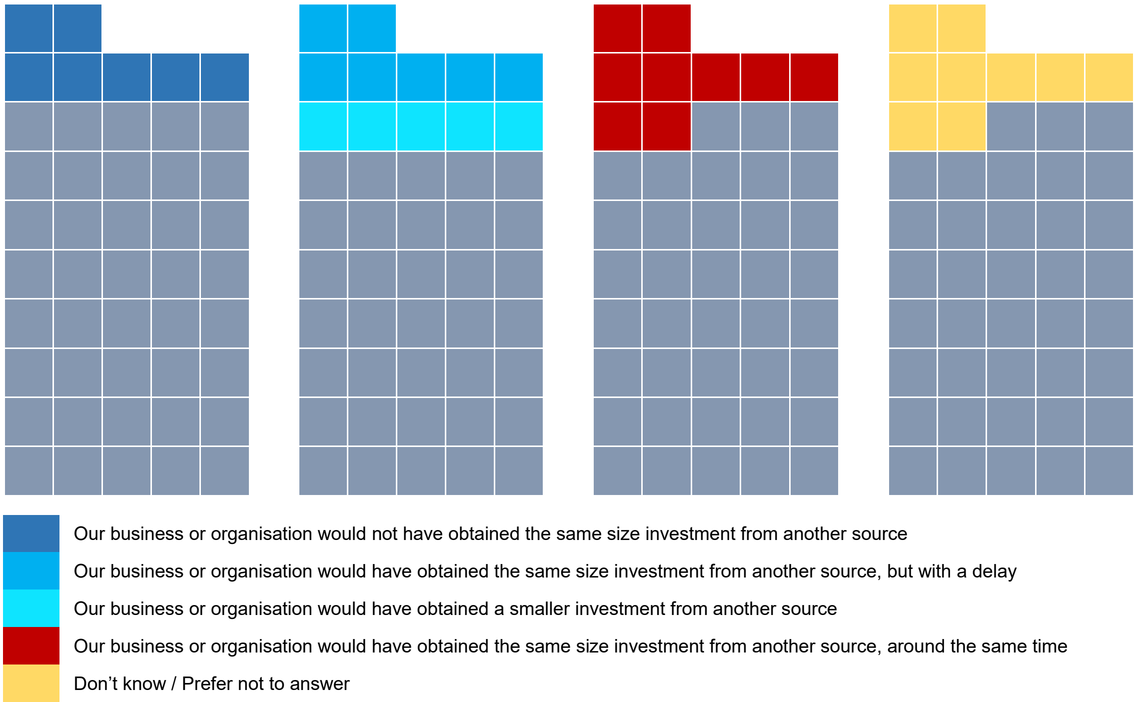
In the survey responses, many fund managers also mentioned that other investors would have contributed less in the absence of the EIF, making their funds even smaller. This is explained by the 10% exposure limit applied as a rule by most institutional investors. Since it is clear that, in all five cases, the funds would have been much smaller without EIF support, those institutional investors applying the 10% rule would have had to reduce their contributions accordingly to stay within their maximum exposure.

Interestingly, all five fund managers who were interviewed stated that a smaller fund size (in the absence of EIF investment) would have negatively affected their ability to attract a skilled team. As one fund manager put it, “a sub-scaled fund is a sub-skilled fund.”

[55] Some of the SIA-backed fund managers hire people who are specifically tasked to support the fundraising process. To compensate for the absence of the EIF, several other (smaller) investors would have had to be convinced. This would have required more fundraising resources, thereby increasing related costs.

The evaluation finds that the additionality of SIA support is slightly weaker at the final beneficiary level (compared to the fund level), but in line with other similar interventions. In their responses to the survey, 21% of social enterprises reported no additionality from SIA-backed funding, meaning that they would have been able to obtain the same volume of finance (as they received from the SIA-backed fund) from other sources on similar terms and conditions and within the same timeframe. This is in line with other similar interventions. For example, in the 2017 Commission survey of final beneficiaries of the COSME Loan Guarantee Facility,[56] 24% of the final beneficiaries would have proceeded with their projects, unchanged and within the same timeframe, without COSME financing.

Figure 23. Additionality of SIA financing at the final beneficiary level



Source: Social enterprise survey, n=42

The lending activities of most financial intermediaries would have been affected in the absence of EREM support. In their responses to the survey, seven of the 14 intermediaries claimed that without the EIF loan, either their SME lending volumes would have decreased or grown only in proportion to capital available, or their loans to SMEs would have had shorter maturities. Three intermediaries indicated that they would have accessed a loan or other investment from another source, but it would have been smaller or on less favourable terms. Only two intermediaries reported that the absence of EIF support would not have affected either their funding or lending activities.

The majority of CBSI reported an increase in their SME lending during 2014-2018, but several factors contributed to this trend. In their survey responses, 12 (out of 14) intermediaries reported an increase in both the value and number of loans to SMEs. Nine intermediaries also indicated that the relative share of SMEs in their overall lending portfolio (by value) had increased during the same period. The intermediaries highlighted several factors contributing to these trends. Demand-side factors (e.g. increase in demand for loans, availability of bankable SMEs) appear to have had a stronger influence than supply-side factors (e.g. the EIF loan, availability of lending capital from other SMEs) on most intermediaries' lending patterns during the evaluation period.

[56] This survey was carried out as part of the Commission's interim evaluation of COSME (359 respondents in total).

4.3 Over 100 000 SMEs, small mid-caps and social enterprises have already benefited from improved access to finance

EREM financing has reached more than 100 000 SMEs, small mid-caps and social enterprises over a five-year period (March 2014 to June 2019), representing 54% of the target of 202 561 final beneficiaries.[57] As the portfolios are still building up, the number of final beneficiaries is expected to change in the coming years. While an increase is expected for some products (e.g. the LFI, the SIA and the CBSI Instrument), self-audits of financial intermediaries' portfolios have already resulted in some exclusions and more are expected in the future (particularly for the SME Initiative). It is nonetheless clear that the envisaged target number of beneficiaries will not be met for the LFI and the SME Initiative Option 2. The reasons are as follows:

- LFI: The actual average ticket size (size of investment) in SMEs and small mid-caps is 6.5 times higher than initially assumed (€1.6 million versus the expected average investment size of €250 000 – see Annex 4 for calculations). This means that a smaller number of SMEs and small mid-caps will eventually be financed compared to the target. Such deviation is understandable because this product is new and market conditions have evolved over time.
- SME Initiative Option 2: The budgetary take-up of the instrument has been much lower than expected, as explained earlier. The low level of absorption is ultimately reflected in the lower than expected beneficiary numbers.

Table 4. Number of SMEs, small mid-caps and social enterprises financed by EREM as of 31 December 2019

	Target*	Actuals up to 31/12/2019	% Target achieved
Social Impact Finance	451	195	43%
Loan Funds Instrument	16 006	1 239	8%
CBSI Instrument	7 410	2 025	27%
SME Initiative Option 1	34 137	53 209	156%
SME Initiative Option 2	63 333	1 050	2%
ABS Credit Enhancement**	81 225	51 430	63%
EREM total	**202 562**	**109 148**	**54%**

* *Target numbers of beneficiaries have been pro-rata adjusted. Actual numbers based on data as of 31 December 2019. These are not the final numbers as the investment/inclusion period has not yet ended.*

** *Data separately provided by the EIF.*

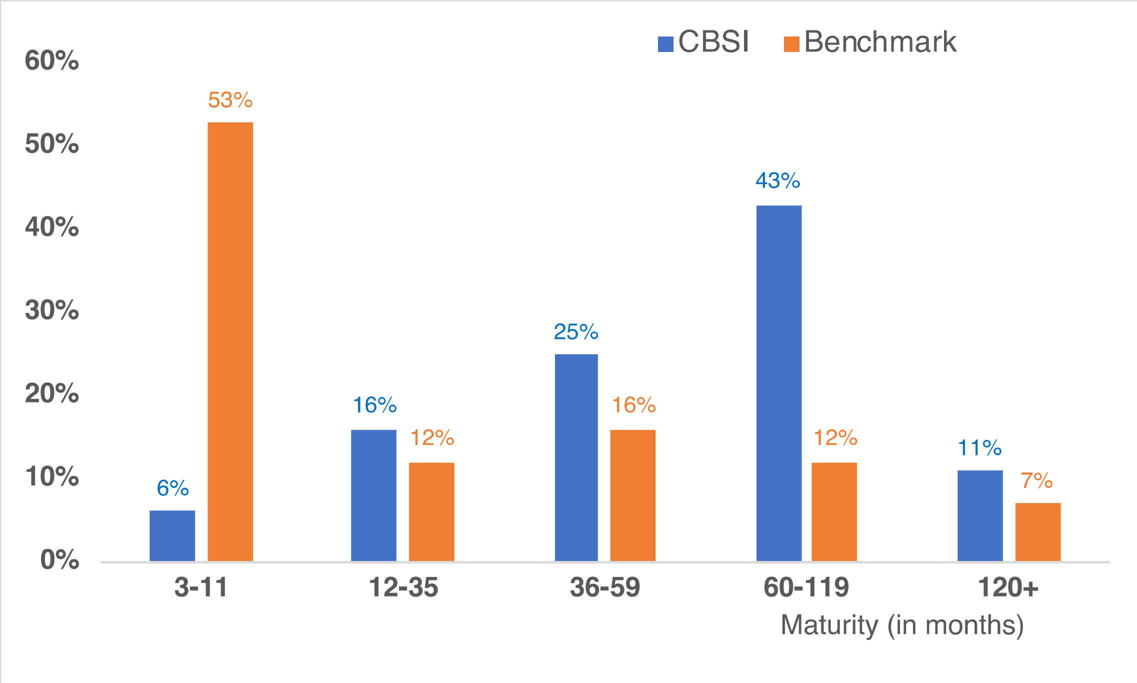
Source: EIF

[57] EREM's initial target of 540 000 beneficiaries for the 2014-2020 period has been adjusted on a pro-rata basis according to the final budget allocation in the first period. The initial targets, pro-rata adjusted numbers and actual numbers of final beneficiaries reported as of December 2018 are shown in Annex 4.

4.4 Aside from the increased volume of financing, the assisted businesses have also benefited from improved financing conditions and non-financial support

The CBSI Instrument has also improved the lending conditions for borrowers. Unlike the Commission mandates (e.g. COSME, L4SME), the CBSI contractual documents did not require financial intermediaries to pass on the benefits of EIF loans to final beneficiaries, for instance by reducing the collateral requirement or interest rate. Nonetheless, EV analysis revealed that CBSI loans typically have a longer maturity than bank loans. As shown in Figure 24, the vast majority of SME loans under the CBSI Instrument have a maturity longer than one year, whereas almost half of the banking sector loans to businesses have a maturity of less than one year. The median maturity of the CBSI-supported SME portfolio is five years.

Figure 24. Distribution of maturity of loans of CBSI-supported SME portfolio vs. banking sector benchmark (euro area)



Sources: CBSI monitoring data (2017-2019); benchmark data sourced from the ECB (volumes of new euro-denominated loans of up to €0.25 million to euro area NFCs; November 2018-November 2019).

Social enterprises receiving investment from the SIA have also enjoyed better terms and other benefits. In their survey responses, several social enterprises indicated that when they had a choice, they preferred the SIA-backed fund over others because investment terms and conditions were more favourable and other benefits were available, such as business advice and support and networking opportunities which facilitated the development of their businesses. Moreover, social enterprises also preferred SIA-backed funds because they were equipped with social investment specialists and better understood their needs.

Loan funds offer better conditions to borrowers than bank financing. Desk research and the survey of fund managers highlighted several advantages of private debt over bank financing, most notably longer tenors, more flexible financing (e.g. bullet repayment structure) and greater speed of financing (several weeks vs. months).

4.5 EREM financing is relatively concentrated in MS with the largest share of EU GDP

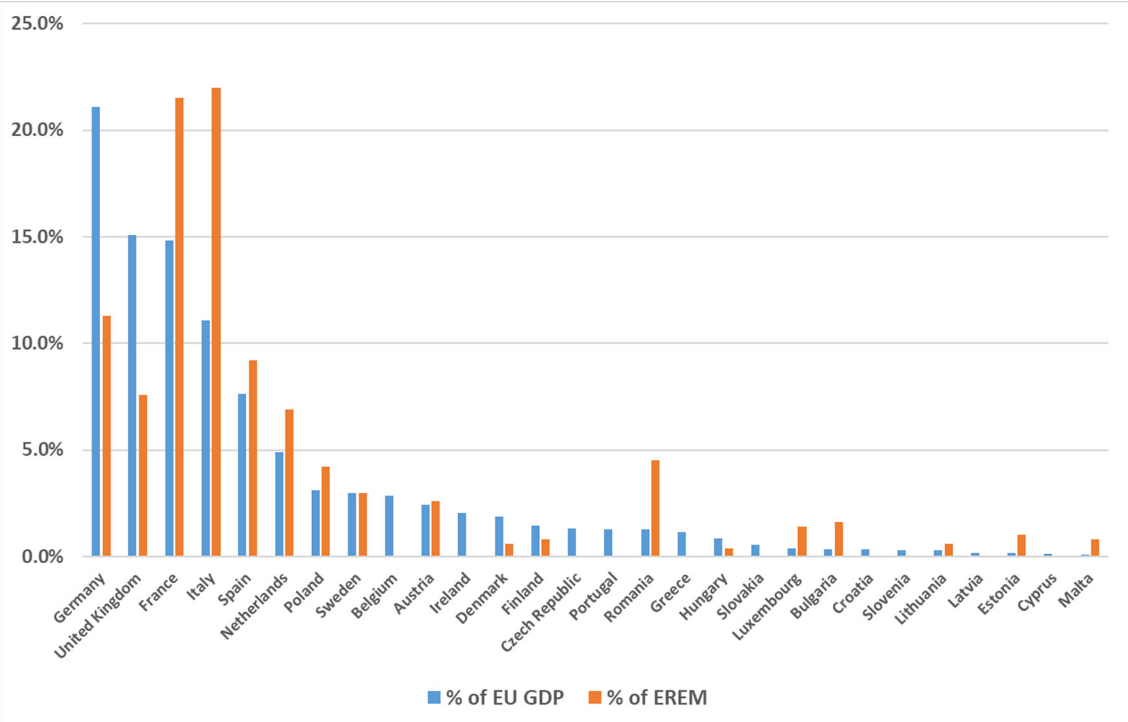
Approximately 80% of EREM commitments are concentrated in six MS (France, Italy, Germany, Spain, the United Kingdom and the Netherlands), representing some 75% of EU GDP.[58] Except for Italy and Spain, access to finance was a relatively low concern among businesses (particularly SMEs) located in these MS. Conversely, there are no EREM commitments in MS reporting significant gaps in access to finance, such as Greece, Latvia, Cyprus and Croatia, while only relatively small transactions have been recorded in some other MS reporting these gaps, such as Romania and Bulgaria**.**

Once economy size is accounted for, Germany and the United Kingdom benefit relatively less, while Romania, Bulgaria, Estonia, Luxembourg, Poland, Italy, France, the Netherlands and Spain benefit relatively more. Nevertheless, even accounting for the size of their economies, some countries with significant gaps in access to finance, such as Portugal and Greece, do not benefit at all. However, with respect to EREM funding in MS, it must be acknowledged that EREM had no specific geographic allocation targets.

Figure 25 shows a comparison of EREM commitments with MS GDP. Additional data on EREM and GDP are presented in Annex 4.

The geographic concentration of EREM is partly driven by differences in the development, funding absorption capacity and sophistication of the markets. Some EREM products, such as the LFI and the SIA, were less suitable for countries whose financial markets are currently less sophisticated, and it was expected that these countries would be covered by other EIF products. Legal restrictions also played a role in limiting the geographical take-up of some products (e.g. securitisation products such as ABS Credit Enhancement). For example, a regulatory framework for loan origination by private debt funds was lacking in several MS (Bulgaria, Greece, Hungary, Poland and Romania), which restricted the take-up of LFI in these countries.

Figure 25. Comparison of EREM commitments with the GDP of MS



Sources: EIF ESAF, ECB SAFE, EIF reporting on EREM, Eurostat

[58] Based on 2018 GDP data.

Indeed, some of the countries reporting significant access-to-finance gaps but receiving no EREM financing were well covered by other EIF financing (see Figure 25)**.** This group included Croatia, Cyprus, the Czech Republic, Greece, Ireland and Portugal. However, Latvia, Slovenia and Slovakia received no EREM financing and a disproportionately low share of overall EIF financing relative to their share of EU GDP and the EU SME population.

The geographical take-up of the SME Initiative was far more limited than initially expected. The slow take-up of the SME Initiative was particularly challenging. It can be explained by the wait-and-see approach of managing authorities, which waited for feedback on how the product works before launching their own initiatives.

The geographical take-up of the CBSI Instrument – a relatively plain vanilla product – shows little alignment with the highest SME needs for access to finance. MS that score very high on SME satisfaction with access to external finance (Sweden, Germany and Austria) have financial intermediaries that signed contracts under the CBSI instrument, while only one of the MS scoring low on this measure (Romania) has financial intermediaries that signed contracts under the CBSI Instrument. No CBSI loans were made in MS where SMEs have a persistent need for external finance (Greece, Cyprus, Croatia and Hungary). It is understood that the geographical placement of the CBSI Instrument was demand-driven and subject to various eligibility and marketing constraints, as discussed in section 3.

For new products such as the SIA and the LFI, the EIF adopted a deliberate strategy of initially focusing on countries where the asset class already existed, and then diversifying to newer markets. The first SIA investments were made in social impact funds located in France, the United Kingdom and Germany. The EIF then gradually expanded to other EU countries where impact investing was non-existent (e.g. the Netherlands, Denmark, Hungary and Spain). Similarly, the first LFI investments were made in the United Kingdom, the Netherlands and France. The product was then introduced to Germany, Spain and Italy. This strategy is largely explained by the demand-driven approach applied by the EIF and is justified on the following grounds:

- The need to build champions by investing in funds located in more established markets to demonstrate the financial viability of the asset class;
- Investments in more experienced funds also created opportunities for the EIF to capitalise and transfer knowledge to other less experienced fund managers. Some of this knowledge (e.g. on monitoring social impact) was transferred via the EIF's structuring input.

4.6 Recap of key messages

- With an investment of €2 billion, EREM is expected to leverage almost €34 billion of financing for SMEs, small mid-caps and social enterprises over a ten-year period (2014-2023). However, not all of this volume of financing leveraged can be attributed to EREM. It is possible that some of this financing might have been provided by the market or other sources even in the absence of EREM.
- For the SIA, the LFI and the CBSI Instrument, though, the evaluation does find evidence of strong additionality. Much of the financing leveraged by these products would not have materialised in the absence of EREM.
- Many of the social enterprises supported under the SIA would not have otherwise been able to obtain the same volume of finance (as they received from the SIA-backed fund) from other sources on similar terms and conditions and within the same timeframe.
- EREM financing reached more than 100 000 SMEs, small mid-caps and social enterprises by mid-2019. As the portfolios are still building up, the number of final beneficiaries is expected to rise in the coming years. It is nonetheless already clear that the target number of beneficiaries will not be met for the LFI and the SME Initiative Option 2.
- Evidence collected for the LFI, the SIA and the CBSI Instrument suggests that aside from an increase in financing volume, the assisted businesses have also benefited from improved financing conditions and non-financial support.
- Approximately 80% of EREM commitments are concentrated in six MS (France, Italy, Germany, Spain, the United Kingdom and the Netherlands), representing some 75% of EU GDP. The geographic concentration of EREM is partly driven by national differences in the development and sophistication of financial markets (for the SIA and the LFI). However, the plain vanilla product of the CBSI Instrument was also concentrated in a limited number of MS. This was due to eligibility constraints that limited the pool of eligible intermediaries and marketing constraints caused by delays in the set-up of the product.
- In several countries, the take-up of products such as the LFI and ABS Credit Enhancement was also limited by legislative restrictions. Meanwhile, the SME Initiative suffered from the wait-and-see approach adopted by several managing authorities.
- For new products such as the SIA and the LFI, the EIF adopted a deliberate and justifiable strategy of initially focusing on countries where the asset class already existed (to build champions and the EIF's own track record and experience) and then diversify to newer markets (market-building role).

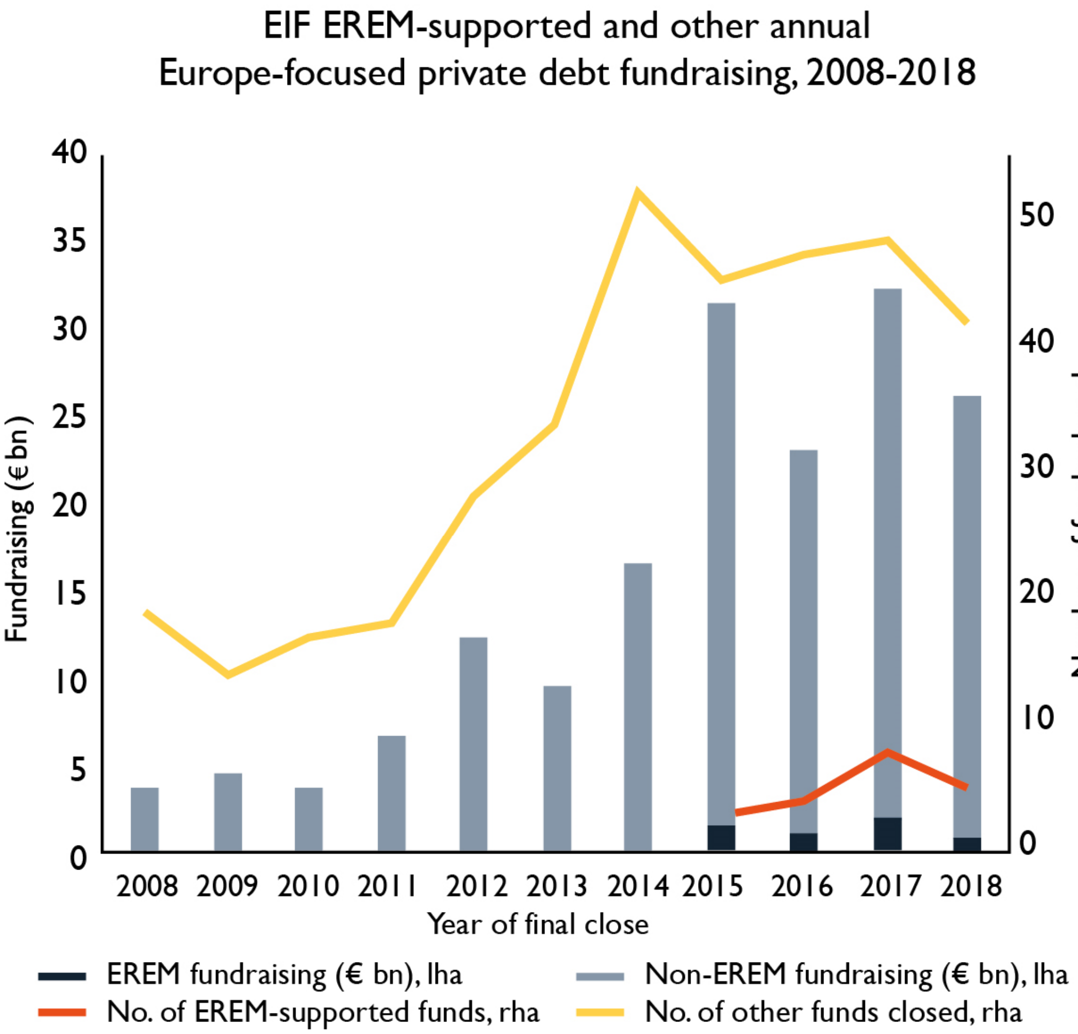
5. Effectiveness in Developing Non-Bank Sources of Finance for SMEs, Small Mid-Caps and Social Enterprises

The market-building role of the EIF was specifically envisaged under the LFI and the SIA. This section assesses the extent to which this objective was achieved. Aside from the EIF's financial investment in intermediaries, there are several other channels through which the EIF could have used EREM resources to develop market infrastructure. For example, the EIF could contribute to widening and diversifying the investor base for a particular asset class by attracting new classes of investors through its signalling effect and by demonstrating the viability of the asset class. The EIF could also develop markets by methods other than investment, such as building new intermediaries by supporting first-time teams or strengthening intermediary capacity by providing structuring support. This section analyses the extent to which the LFI and the SIA contributed to building market infrastructure for direct lending and impact investment, respectively. For the SIA, the evaluation also examined if the EIF played any role in developing and facilitating progress towards shared norms for measuring and managing impact or developing new instruments, mechanisms or practices, such as the impact-based carry approach.

5.1 The LFI planted the seeds for developing the lower mid-market segment of the private debt industry in Europe

The EIF's financial investment in intermediaries (via EREM) has been crucial in supporting the development of the private debt industry in Europe focusing on the SME and small mid-cap segment. The EIF has been one of the first and largest institutional investors in this space. During the LFI implementation period (2015-2018), EREM loan funds represented an estimated 20% of fundraising focusing on the SME and small mid-cap segment through direct lending and mezzanine strategies (see Figure 26). EREM thus represented a critical share of all fundraising efforts. Moreover, as reported in section 4, the EIF often came in at first closing and supported 11 first-time teams, thus expanding the scale and diversity of funds operating in the lower mid-market segment.

Figure 26. Annual Europe-focused private debt fundraising, 2008-2019



Notes: Supported loan funds represented 5% of the total Europe-focused private debt fundraising (Preqin data). However, Preqin data cover all different fund strategies, such as direct lending, mezzanine, distressed debt, special situations and venture debt, whereas the EREM intervention only included direct lending and mezzanine. These two strategies combined represent roughly 50% of the total private debt fundraising (correction factor x2). Moreover, according to the European Systemic Risk Board (ESRB, 2019), lending to SMEs and small mid-caps, which was the focus of EREM, accounted for approximately half of the lending provided by private credit markets (additional correction factor x2). Accordingly, it is estimated that EREM represented 20% (=5%x2x2) of the relevant fundraising.

Sources: EV calculations using EIF data and Preqin Pro data

The EIF's presence had a strong signalling effect for other investors, which has been critical for developing the lower mid-market segment of the asset class. All fund managers who responded to the survey (15 out of 17) stated that the EIF's investment signalled the quality of their fund to other investors. A further 10 fund managers confirmed that the EIF's investment had attracted new categories of investors who would otherwise not have invested in this asset class (see Table 5.

Table 5. Transaction-level impact of the LFI

Q: To what extent do you agree or disagree with the following statements about the added value of the EIF's investment in your fund?

	Strongly agree	Agree	Disagree	Strongly disagree	Don't know / Prefer not to answer	Total number of responses
Signalled the quality of the fund to other investors	**11**	**4**	**0**	**0**	**0**	**15**
Attracted new categories of investors who would otherwise not have invested in this asset class	5	5	3	0	2	15
Increased the size of the investments that other investors were willing to make	**7**	**7**	**1**	**0**	**0**	**15**
Reduced the amount of due diligence that other investors undertook	2	5	2	1	5	15
Increased your investment strategy focus on SMEs / small mid-caps	6	4	4	0	1	15
Demonstrated stability in the investor base	**7**	**7**	**1**	**0**	**0**	**15**

Source: Survey of loan fund managers, n=15

The case studies provided further evidence that the presence of the EIF had a strong signalling effect for other investors, allowing the funds to attract additional third-party investors, both from the public (national promotional institutions and banks) and the private sector (mainly pension funds, insurance companies and high-net-worth individuals). In an industry with a strong domestic bias among investors, the EIF's support is also claimed to have encouraged investors to invest across borders.

Anecdotal evidence from a few interviewed managers of funds not supported by EREM highlighted the considerable (and growing) role of the EIF in developing the lower mid-market segment of the asset class. Whereas the upper mid-market segment has attracted extensive capital, funds operating in the lower mid-market face greater challenges in fundraising. Some large limited partners (pension funds and insurance companies) do not even consider investing in the lower mid-market as they have investment restrictions in terms of minimum ticket size (> €100 million) and maximum shareholding (< 10%), and consequently favour funds whose size is > €1 billion. These larger funds, due to their size and need to deploy capital in a timely manner, tend to focus on larger tickets from mid to large corporates, and less on SMEs and small mid-caps. The EIF's role and signalling effect is thus perceived to be more critical in this segment of the market.

The EIF has also contributed to developing the private debt industry through its rigorous due diligence and high-quality structuring input. A review of the project documentation revealed that the EIF's structuring input cut across a number of aspects. Contributions to the governance (e.g. composition and functioning of investment committees) and overall mission of the funds were more frequently observed than inputs regarding the management structure. In the view of the evaluation team, the due diligence notes produced by the EIF were very thorough and comprehensive.

The evaluation also collected feedback from fund managers on the usefulness of the structuring support provided by the EIF. Of the fund managers who responded, just over half (eight out of 15) acknowledged having received the EIF's structuring input and they unanimously rated it as very useful and reported having made changes to their funds as a direct result of this input. The quotes below provide a flavour of the types of changes made by fund managers in response to the EIF's structuring input and the resulting benefits. The main changes reported by fund managers related to fund governance, including team composition, better alignment of interests (conflict of interest policy), more detailed reporting and fund remuneration. Some of the changes affect the remuneration of fund managers and/or aim at ensuring a closer alignment of their interests with those of investors (i.e. requiring fund managers to have more skin in the game).

Nevertheless, most of the responding fund managers saw the changes required by the EIF as positive, as these changes were in line with industry practice and provided comfort and reassurance to other investors. The EIF's status as a cornerstone investor seems to have made the fund managers more willing to accept the EIF's requirements.

"The EIF helped to better shape the fund's governance by clearly detailing the roles and duties of the management team, investment committee and advisory board."

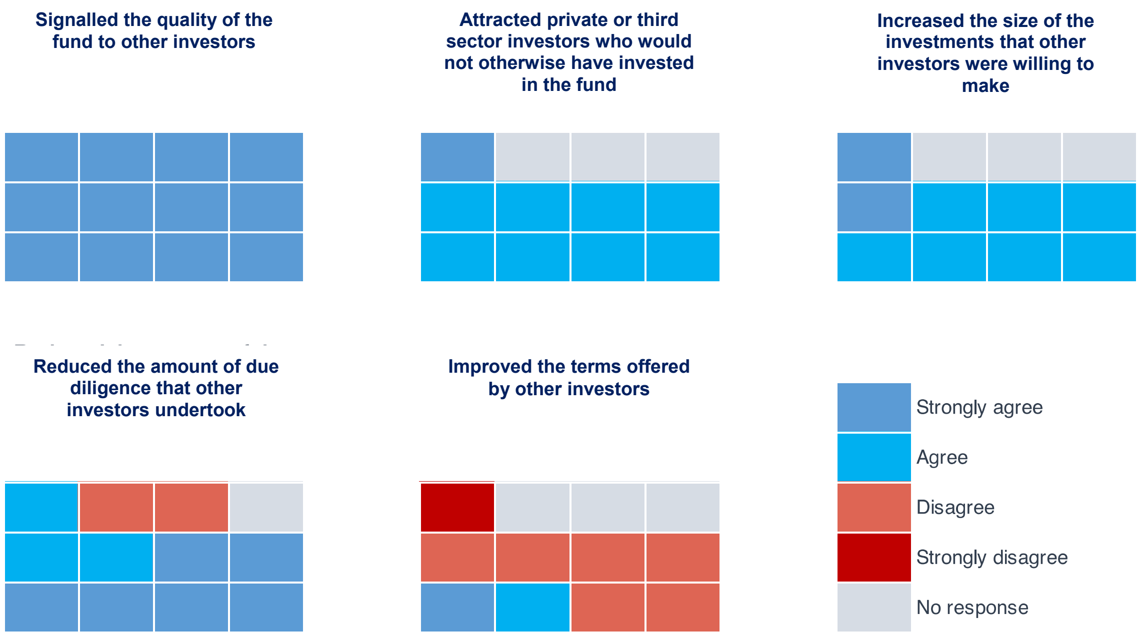
"The EIF asked us to introduce a split management fee comprising (a) a fee levied and paid to the manager quarterly and (b) a fee levied quarterly but paid upon reaching a certain performance target."

Interviewed fund managers also typically highlighted due diligence as the specific EIF input with the highest added value. One fund manager described it as "tough and going beyond what other investors would ask for, but at the same time extremely useful". Other fund managers viewed it similarly. Overall, the EIF's due diligence was found to be equally helpful for first-time and established funds. Anecdotal evidence from the interviews also suggests that the EIF's due diligence is seen by the market as considerably more thorough than what other investors do.

5.2 Role of the SIA in building impact investment markets

The SIA had a strong catalytic effect at both transaction and market levels. In their responses to the online survey, all 12 fund managers strongly agreed that the EIF investment signalled the quality of their fund to other investors. Fund managers also confirmed that the EIF's presence attracted private investors who would not otherwise have invested in the fund and that other investors reduced their due diligence because the EIF was involved (see Figure 27). Similar to its approach through the LFI, the EIF often came in at first closing and supported five first-time teams (out of a total of 12), thus expanding the scale and diversity of funds operating in the European impact investment space.

Figure 27. Transaction-level impact of the SIA



Source: Survey of SIA-backed fund managers, n=12

The signalling effect of the EIF was further evident in all five funds selected for case studies. Interviewed fund managers explained that this is largely due to the EIF's reputation as a large, professional organisation with a proven track record (in venture capital and private equity) and pan-European scale and experience, which make the EIF well trusted among investors. This trust means that smaller organisations (such as some family offices) which either lack capacity for thorough due diligence or do not see the need for it are more willing to invest in a fund if the EIF is present.

However, the interviews revealed that the EIF's presence alone is not sufficient to convince other investors. While the EIF's presence has clearly helped in the fundraising process, investors also need to have confidence in the team managing the fund and in the fund's mission and objectives before deciding to invest. In the words of one fund manager: "[the] EIF's commitment comes as a reassurance once there is initial interest. Going forward, it could be a way of selection for investors not able to conduct impact [due diligence] on their own. That being said, [the] EIF's commitment is clearly an attractive factor once an investor adheres to the vision, as its decision remains linked to the size of the fund and the quality of the team."

The small number of interviewed co-investors further corroborated the fund managers' claims on the EIF's signalling effect. These investors agreed that the EIF's presence had signalled the quality of the funds to them. They believed that the EIF's depth and breadth of experience in the venture capital field meant that "they are a serious organisation and take seriously any fund they invest in". However, these investors also said that they would have invested in those funds anyway, and would have done the same level of due diligence as normal, despite the EIF's presence. Overall, they emphasised that the EIF's presence had provided them with extra confidence and comfort.

The above analysis suggests that the EIF acted as a catalyst and significantly helped the fund managers in their fundraising process. Nevertheless, the evaluation also looked for cases where the EIF's presence may have unintentionally crowded out other investors. This was assessed using two different angles of analysis:

- Whether the sheer size of EIF investments may have resulted in the funds reaching a size considered excessive by some investors, thereby dissuading them from investing in the funds;
- Whether some of the governance changes induced by the EIF via its structuring input or the association of the EIF with public sector funding may have put some investors off.

The evaluation found no evidence to support either hypothesis. Documentation review and case studies suggest that the EIB Group was conscious of the potential risk of crowding out other investors through its activities and managed this risk appropriately:

- The SIA allowed for investments of up to 49.9% of a fund's shareholding. SIA participation reached 49.9% in only four of 14 cases; in all the other cases it was significantly below this level (20-35%). In all four cases where the SIA investment was 49.9%, the fund managers were clearly struggling to reach the minimum size.
- The funds which closed at a higher size typically had lower SIA participation. Some of the more prominent SIA-backed funds received considerably lower SIA investment given their capacity to attract investors.
- There were no cases where investor commitments were subject to a maximum size limit on the fund. On the contrary, investors typically committed subject to a minimum fund size to avoid spreading their resources too thinly over a large number of funds, which would, in turn, result in high management costs for the investors.

The survey of fund managers also explored the catalytic role of the SIA at the market level (see Table 6). All fund managers "agreed" or "strongly agreed" that the EIF investment had amounted to a step change in the size of the impact investment market in their country and that it had catalysed existing investors to invest more in this asset class. Many fund managers also mentioned that the EIF had attracted new investors to the asset class, thus widening and diversifying the investor base. One fund manager put it as follows: "[the] EIF chooses where it puts its capital. That itself is a signal to the market about impact investing."

Table 6. Market-level impact of the SIA

Q: To what extent do you agree or disagree with the following statements about the impact of the EIF's investment in [Fund_name] on the wider social impact investment market in your country?

	Strongly agree	Agree	Disagree	Strongly disagree	Don't know / Prefer not to answer	Total number of responses
Amounted to a step change in the size of the social impact investment market in [Country_name]	**10**	**2**	**0**	**0**	**0**	**12**
Catalysed existing investors to invest more in the social impact investment market than they would otherwise have done	**7**	**5**	**0**	**0**	**0**	**12**
Encouraged new private and third sector investors to enter the social impact investment market (crowding-in)	4	4	1	0	3	12
Catalysed public sector support to the social impact investment market (investment, policy support)	3	4	2	0	3	12
Improved the credibility of the social impact investment sector	**7**	**5**	**0**	**0**	**0**	**12**
Helped establish social impact investment as a recognised asset class	**4**	**7**	**0**	**0**	**1**	**12**
Helped establish and promote best practice and standards (in measurement of impacts, in the use of financial incentives)	**5**	**5**	**1**	**0**	**1**	**12**
Broadened the range of investment products available to social enterprises	4	4	2	0	2	12

Source: Survey of SIA-backed fund managers, n=12

The structuring input provided by the EIF has helped to improve the governance and professionalism of supported funds. The EIF typically provided structuring input (defined as a form of advice) on a wide range of governance and investment decision-making aspects under the SIA. Survey responses from the SIA-backed fund managers suggest that most funds received structuring input from the EIF and the vast majority of those that did found the EIF's input to be very useful. These fund managers also reported having introduced changes as a result of the EIF's structuring input. Examples of such changes include:

- Improving the monitoring of social impact;
- Restructuring management teams;
- Introducing incentive schemes to improve the alignment of interests between the fund manager and investors;
- Sharpening the fund investment strategy, including focus on social impact;
- Introducing key-person clauses to limit staff turnover;
- Strengthening the independence of the management team.

The structuring input provided by the EIF was generally appreciated as bringing professionalism. This applies for all fund profiles but particularly for first-time teams. Five of the 14 SIA-backed funds were managed by first-time teams; as such, the SIA encouraged new teams to join the impact investment market and provided them with critical advice. One exception to the otherwise positive assessment (which does not offset the benefits from EIF involvement) is the inflexibility of some specific requirements: for example, the strict key-person clause was intended to limit the risk of key staff turnover but did not foresee problems such as force majeure circumstances.

The EIF's social impact performance methodology (applied in its original form or adapted) has been promoted through the SIA, thus contributing to progress towards shared norms for measuring and managing impact. The SIA focus on impact measurement has been appreciated, given that other investors, despite being committed to impact, typically lack the expertise to go deep into the methodological debates and impact measurement issues. The case studies provide strong evidence that, without the SIA methodology, considerably less attention would have been paid to social impact monitoring. The fund managers agreed that the quality of monitoring would have been lower and, more generally, there would have been less clarity on how the supported enterprises seek to deliver social impact.

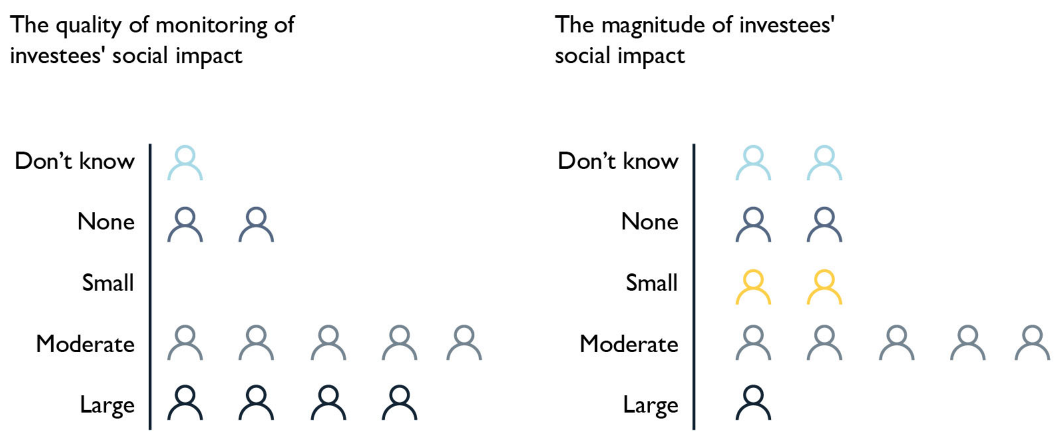
Box 6. Social impact performance methodology

The social impact performance methodology of the SIA involves the fund manager committing to a number of specific tasks to measure and report on the impact achieved by portfolio companies. In coordination with the fund manager, portfolio companies are asked to define one to five social impact indicators and set a pre-investment target value for each indicator. Fund managers then disclose the social impact indicators and pre-investment target values to their investors and regularly calculate (at least once per year) the impact multiple, calculated by comparing the pre-investment target and realised value. Impact multiples must be reported at least once per year. The financial performance incentive of the fund manager (carried interest) is subject to the social impact performance of the fund.

In parallel, the EIF also contributed via the SIA to developing the impact-based carry mechanism. This mechanism stipulates that a fund manager is entitled to receive the carried interest (an additional form of remuneration) only if, in addition to achieving financial performance surpassing a predetermined hurdle rate, the fund also achieves certain social impact targets. Nine of the 12 fund managers believed that the impact-based carry mechanism has had a moderate or large impact on the quality of social impact monitoring. However, the fund managers were less convinced that the mechanism has affected the magnitude of social impact achieved by their investees.

Figure 28. Effects of the impact-based carry mechanism on SIA-backed funds

Q: What impact (if any) did the social impact financial incentives used by the EIF have on the following aspects of the delivery of the fund?



Source: Survey of SIA-backed fund managers, n=12

None of the case studies provided evidence that the impact-based carry mechanism incentivised fund managers to push for higher social impact than they would have otherwise pursued. This was primarily because the fund managers were already very committed to supporting investee companies to achieve social impact. Also, the achievement of social impact was mostly attributable to the self-motivation and enthusiasm of the social entrepreneurs. However, the case studies suggest that the impact-based carry mechanism improved the quality of the monitoring of social impact[59] and had other positive effects, such as enhancing the credibility of fund managers in the eyes of other investors and of their investees. The fund managers also reported that the enhanced attention to monitoring caused social entrepreneurs to focus their minds on the impact they had promised to deliver, rather than taking it for granted. Conversely, one interviewed investor argued that the impact-based carry mechanism potentially acts as a perverse incentive for fund managers to "fudge" targets, i.e. to set them too low so they can easily be met. However, the evaluation found no evidence to support this claim.

5.3 Recap of key messages

- The EIF has contributed to widening and diversifying the investor base in the lower mid-market segment of the European private debt industry and the impact investment space by attracting new classes of investors to these asset classes. In the private debt sector, the EIF has pulled in institutional investors, public sector investors and high-net-worth individuals. In the impact investment space, there is evidence that the EIF's presence catalysed investment from family offices, particularly smaller ones.
- The EIF has also contributed to developing these markets through methods outside investment, such as building new intermediaries by supporting first-time teams and strengthening intermediary capacity by providing structuring support. The structuring input provided by the EIF was appreciated by fund managers and resulted in positive changes.
- The SIA has played a key role in establishing and promoting industry standards and best practice in the areas of social impact measurement and reporting, and of impact-based carry.
- The impact-based carry mechanism is, however, not perceived as having influenced the social impact delivered by assisted funds. Its main added value has been to help maintain focus on social impact and to strengthen monitoring.

59 Note the caveat that the monitoring data are not independently verified (given the absence of a common methodology for conducting such audits and the costs associated with independent audits).

6. Efficiency Considerations Factors affecting Implementation

This section discusses the main factors affecting the implementation of EREM.

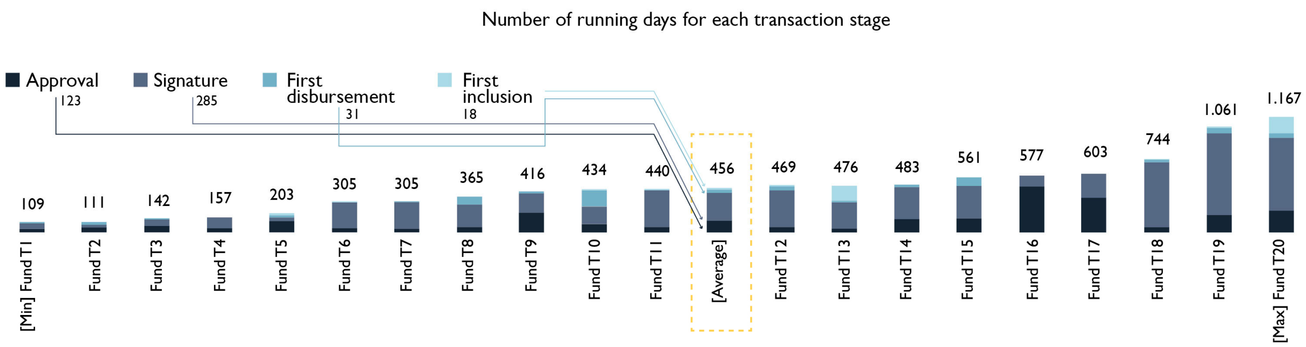
6.1 There were considerable delays in getting the money from EREM flowing into the real economy

Several EREM products took a long time (over two years) to reach their first beneficiary. For example, the loan funds took on average around one year and three months (456 days) to reach their first final beneficiary (first inclusion); when added to the one year and one month necessary to set up the LFI Agreement, the time taken to reach the real economy was nearly 2.5 years. As the analysis below shows, the main reason for the delay was the lengthy fundraising process at the transaction level:

- Time to approval represents the running days between the appraisal authorisation and EIF Board approval, which for EREM loan funds averaged around four months (123 days). This is roughly in line with that for EFSI operations (as per the June 2018 evaluation of EFSI).
- The time required to sign the fund's subscription agreements averaged around 9.5 months (285 days), depending on the fund manager's ability to attract other investors (fundraising process) willing to commit a minimum threshold enabling the fund to close and start operations. When compared to venture capital fundraising, where the rule of thumb is six months of fundraising, this is rather long.
- First disbursements (from the EIF to loan funds) and first inclusions (from loan funds to final beneficiaries) happened relatively quickly, averaging 31 and 18 days, respectively.

There were also some inefficiencies resulting from the budget reallocation process, which created a substantial workload for the EIB and EIF services and caused significant setbacks in instrument readiness and time to market. For example, changes had to be approved by both the EIB and EIF hierarchies, as a result of which it took six months to approve the budget reallocation between the SME Initiative and the LFI (one BoD approval, two MC approvals, one EIF Board approval and one EIF chief executive approval), which effectively froze all LFI transactions during this period.

Figure 29. Time to market for loan fund transactions



Source: EV based on data sourced from LFI transaction documentation

Similarly, it took over three years for financing from the CBSI Instrument to reach final beneficiaries. The CBSI Agreement between the EIB and the EIF was signed in November 2016, more than 2.5 years after EREM was launched (March 2014). Individual contracts between the EIF and financial intermediaries were signed between December 2016 and March 2018, while disbursements to final recipients began in January 2017. The CBSI Instrument had the potential to be delivered relatively quickly considering the plain vanilla nature of the instrument (i.e. senior unsecured loans) and the prior experience of the EIB Group (EIB and EIF) with intermediated lending to SMEs.

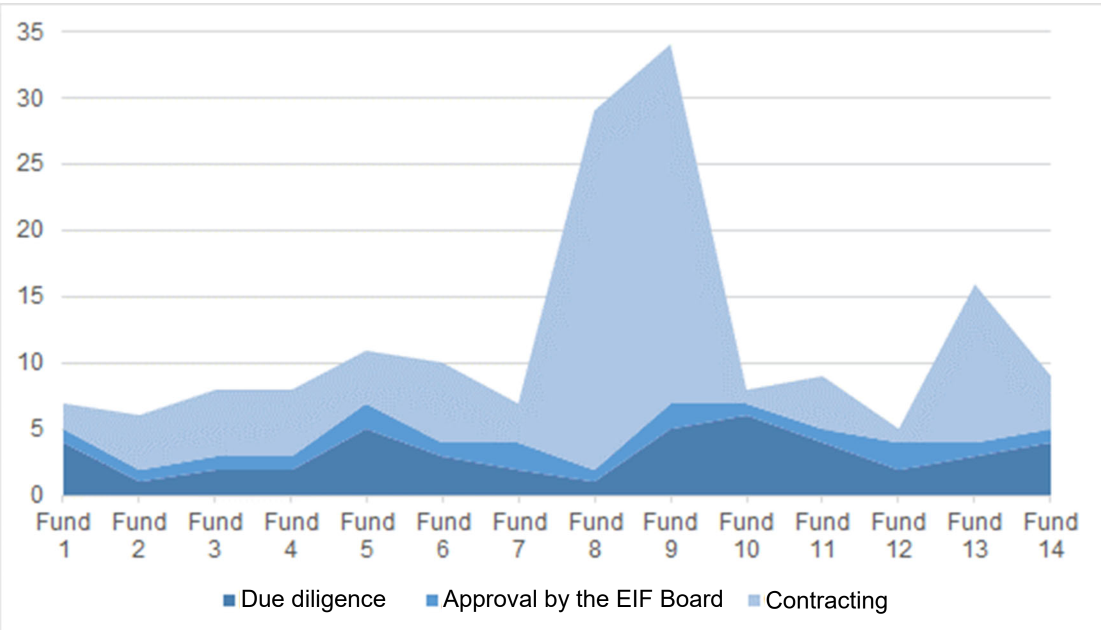
Desk research shows that the delay in signing the CBSI Agreement was caused mainly by:

- Long discussions between the EIF and the EIB around the delivery model to be adopted – shared EIB and EIF administration versus full delegation of product implementation to the EIF – and a change in the originally intended approach midway through the instrument set-up process;
- The decision to stagger the launch of EREM instruments so as not to exceed implementation capacity.

Finally, as mentioned in section 3, the SME Initiative also took a rather long time to develop but this was due to factors outside the EIF's control, such as the complexities created by the involvement of several risk-takers and the wait-and-see approach adopted by many managing authorities.

By contrast, the SIA was relatively quick to reach the market. This was because EREM was used to top up an existing pilot product for which processes, procedures and a pipeline were already in place. Moreover, despite being very rigorous, the due diligence process under the SIA was conducted relatively swiftly. On average it took 3.1 months to conduct due diligence of an SIA-backed fund. Approval of transactions was also fairly swift, averaging 1.2 months. However, it took a relatively long time to sign agreements with fund managers: the average time lag between transaction approval by the EIF Board and signature of the agreement with the fund manager was 7.5 months (although the average is heavily influenced by two transactions for which it took more than two years to sign the contract). For some transactions, it actually took longer to sign the agreement with the fund manager than it took to conduct due diligence and get EIF Board approval. Some of the interviewed fund managers confirmed that while due diligence on and approval of transactions were swiftly conducted, the delay before signing the contractual documentation was longer than they would have expected. Fund managers suggested in interviews that this was due to insufficient capacity within the EIF's legal department to handle an increasing number of transactions.

Figure 30. SIA transactions: time taken at different stages (due diligence, EIF Board approval, signature of agreement with the financial intermediary), number of months



Source: EV based on data sourced from SIA transaction documentation

6.2 The partial delegation of the CBSI Instrument created several operational challenges

Co-management of the CBSI Instrument by the EIB and the EIF created several operational challenges and inefficiencies. The initial plan was to fully delegate the CBSI Instrument to the EIF in line with the rest of the Mandate, particularly because the product envisaged loans with much smaller ticket sizes than a standard EIB loan. However, it became clear during the product development phase that the EIF's systems and processes were not fully geared up for a direct lending product[60] and communication with EIB systems. With full delegation thus impracticable, the product had to be jointly managed, which created the following issues:

- As the lending process for the CBSI Instrument was conducted in parallel at the EIB and the EIF, the product documentation had to be adapted. It took six months to one year for the EIF to negotiate waivers and financial covenants as these had to be reviewed and approved by several EIB departments as part of the EIF's standard processes.
- The CBSI Instrument had to be implemented through the EIB's IT system (RASA). During the data interpretation workshop it was revealed that the EIF received limited support to familiarise themselves with RASA, which increased the need for ad hoc support further down the line. Moreover, data had to be manually entered by EIF staff on EIB systems.
- The 95% (EIB) and 5% (EIF) capital split rule[61] created a heavy burden for all parties involved (financial intermediaries, EIB and EIF). It required all documentation and processes to be produced twice (e.g. two invoices originated, two payments made).

6.3 Capital consumption of the Mandate was within set limits, despite its intrinsically high capital intensity

The capital consumption[62] of the Mandate was capped from the onset to a CAR impact of 0.5% or a €1.3 billion volume limit.[63] The overall capital intensity of the Mandate was intrinsically high due to the nature of the products involved. For example, EREM included several high-risk equity and debt products (such as ABS Credit Enhancement with specific and very clear rating limitations and no first-loss tranches).

The actual capital consumption of the Mandate was managed within limits set out from the beginning, even though budgets were partly reallocated to capital-intensive products such as the LFI. Several factors contributed to this:

- *Availability of external ratings for some ABS transactions*: Without an EIF regulatory-compliant internal risk model, these transactions require full capital deduction under the Bank's advanced internal ratings-based approach. In principle, to use the internal ratings-based approach for a securitisation, a bank needs to demonstrate that it has the necessary information to calculate the capital absorbed on all underlying exposures (the "supervisory formula"). The availability of external ratings for some ABS transactions thus reduced the capital consumption of the product (although it should be noted that external ratings for synthetic unfunded securitisation transactions structured for capital relief purposes are extremely rare or unseen).

60 It is noted that the EIF developed a specific loan module in its investment software for the implementation of the European Progress Microfinance Facility - Fonds Commun de Placement, a funded instrument for microfinance, successfully deployed during 2010-2016.

61 This refers to the allocation of EREM sources of funds: 95% EIB and 5% EIF.

62 The capital that needs to be set aside to meet regulatory requirements. Although the EIB is not subject to banking regulation, it voluntarily complies with Best Banking Principles. In line with this approach, the EIB Group calculates its internal capital requirements in accordance with the Capital Requirements Regulation.

63 The €2.8 billion of the budget allocated to the first period of EREM corresponded to a €1.3 billion regulatory capital requirement, based on a bottom-up analysis of the capital requirement per product given the estimated volume for each product.

- *Diversification of equity funds*: A more diversified portfolio represents a lower risk than a less diversified portfolio.
- *SME Initiative Option 1 (Spain)*: More beneficial capital treatment of these exposures was possible by obtaining external ratings.

Less positively, the volume of capital deployed under EREM was eventually lower than the approved budget, which also contributed to reducing the capital consumption of the Mandate.

6.4 Recap of key messages

- The launch and deployment of several EREM products was delayed for various internal and external reasons. Internal factors included lengthy internal discussions between the EIB and the EIF regarding the delivery model for the CBSI product, the length of time taken to approve transactions and sign agreements with financial intermediaries (SIA), and processes involved in budget reallocations (LFI). External factors included the length of time taken for fundraising (LFI) and the wait-and-see approach adopted by managing authorities (SME Initiative).
- For the SIA, using the EREM budget to top up an existing pilot product helped to reduce time to market as processes, procedures and a potential pipeline of deals were already in place.
- The partial delegation model of the CBSI Instrument created several operational challenges and inefficiencies, such as amendments to EIF product documentation in line with the EIB's requirements, manual double entry of transaction data on EIB systems by EIF staff, and the need to split documents and processes to meet the 95:5 resource split requirement.
- Despite budget shifts to relatively high capital-intensive products, the overall capital consumption of EREM was within set limits, primarily due to the availability of external ratings for some transactions.

7. Conclusions and Recommendations

This section sets out the key conclusions of the evaluation and provides a series of recommendations to take into account when designing future mandates of a similar nature. While the evaluation covers the entire Mandate, some aspects (especially questions relating to effectiveness) focus only on the SIA, the LFI and the CBSI Instrument.

7.1 Evaluation conclusions

EREM relevance

- **EREM was conceived in a highly uncertain and fragile economic context, which required a quick and decisive response. The design of the Mandate was, however, not well suited to its (implicit) objective of quickly getting money flowing into the real economy.** It was overly complex, consisting of several novel products which either represented new asset classes (e.g. private debt funds, impact investment) or targeted new types of intermediaries (e.g. CBSI) or final beneficiaries (social enterprises for the SIA). Even some of the relatively straightforward EREM products turned out to be more complex than anticipated. Consequently, the time to market for several EREM products was relatively long (over two years), and by the time EREM was up and running, financing conditions for businesses had considerably improved in most MS and, in parallel, there were other developments such as the EIF's capital increase and the launch of EFSI.
- **The final design of the Mandate (in terms of product choice) was more aligned with its longer-term structural objectives than with its short-term objective of quickly getting money to SMEs.** There is no concrete evidence to suggest this resulted from a deliberate strategy based on due consideration of trade-offs between the one short-term and two longer-term objectives. It is, nonetheless, plausible that as financing conditions improved following the launch of EREM and the EIF's capital increase, there was less urgency to get money into the real economy, leading to the Mandate's structural objectives gaining prominence.
- **Nevertheless, some EREM products were still highly relevant given (a) the persistent financing gaps in some MS and (b) the Mandate's objective of developing non-bank sources of finance for social enterprises, SMEs and small mid-caps.** Overall, the Mandate was still relevant as financing constraints persisted in some MS (e.g. Spain, Portugal, Latvia and Cyprus) throughout the EREM implementation period**.** Moreover, from a medium to long-term perspective, it was justified to support the development of new asset classes and new types of financial intermediaries with the overall objective of diversifying the sources of finance available to social enterprises, SMEs and small mid-caps. This objective was also aligned with the Commission's Action Plan on a Capital Markets Union published in September 2015 which, among other aims, sought to broaden the range of financing options available to businesses. As such, some EREM products (SIA, LFI and CBSI Instrument) were highly relevant. Furthermore, the SIA and the LFI also addressed structural gaps in access to finance for certain types of businesses (e.g. social enterprises) and investment needs (e.g. event-driven transactions, hiring of personnel and overseas expansion). There was, therefore, a particularly strong rationale for including the SIA and the LFI within the Mandate.
- The **strong take-up of some EREM products further illustrates their relevance**. There was very strong market demand for the LFI, in response to which its budget was increased by a factor of six. There was also strong take-up of products such as the SIA and ABS Credit Enhancement. The budget allocated to these products has been fully absorbed. By contrast, demand for the CBSI Instrument and the SME Initiative fell short of expectations for various reasons, including design complexity and marketing constraints.
- **EREM experience has demonstrated that:** (i) it takes time to develop new products; (ii) it takes time to deploy new products in the market as the EIF needs to build its own track record and experience, while concurrently engaging in pipeline building and market development; (iii) for products representing new asset classes, there is an inherent geographical bias in the take-up of resources during the early stages of product launch: MS with relatively more developed or sophisticated financial markets tend to benefit more

than MS with less developed financial markets, even though businesses in the latter countries might have more pressing financing needs; (iv) topping up existing products for which processes, procedures and a potential pipeline of deals are already in place accelerates delivery (this was evident for ABS Credit Enhancement and the SIA).

EREM effectiveness in enhancing access to finance for SMEs and small mid-caps

- **EREM financing has reached more than 100 000 SMEs, small mid-caps and social enterprises so far**. As the portfolios are still growing, the number of final beneficiaries is expected to rise in the coming years. It is nonetheless already clear that the target number of beneficiaries will not be met for the LFI and the SME Initiative Option 2.
- **The SIA and the LFI have proven to be particularly effective in leveraging additional financing for social enterprises, SMEs and small mid-caps.** During the 2015-2018 period, the LFI invested €761 million in 20 loan funds located in six MS. This investment has leveraged €4.8 billion of financing for SMEs and small mid-caps (x7 leverage). Under the SIA, the EIF has invested €148 million in 14 impact funds located in eight MS. This has leveraged €580 million of financing for social enterprises (x4 leverage). Much of this financing would not have materialised in the absence of EREM support. On the downside, these products were heavily concentrated in a few MS. However, the EIF's strategy of initially focusing on countries where the asset class already existed (to build champions and the EIF's own track record and experience), and then diversifying to newer markets (market-building role) was justified under EREM.
- **Without EREM, much of the financing leveraged by the SIA, the LFI and the CBSI Instrument would not have materialised.** Many of the social enterprises supported through the SIA would not have been able to obtain the same volume of finance (as they received from the SIA-backed fund) from other sources on similar terms and conditions and within the same timeframe. Evidence collected for the LFI, the SIA and the CBSI Instrument suggests that aside from an increase in financing volume, **the assisted businesses have also benefited from improved financing conditions and non-financial support**.
- **Overall there is a geographical concentration of EREM financing.** While it is acknowledged that EREM did not have any geographic allocation targets, approximately 80% of EREM commitments are concentrated in six MS (France, Italy, Germany, Spain, the United Kingdom and the Netherlands), representing some 75% of EU GDP. There are no EREM commitments in several MS reporting significant access-to-finance gaps. While some of these countries were well covered by other EIF financing (namely Croatia, Cyprus, the Czech Republic, Greece, Ireland and Portugal), Latvia, Slovenia and Slovakia have received no EREM financing and a disproportionately low share of overall EIF financing relative to their share of EU GDP and the EU SME population. This can be somewhat explained by factors outside the EIF's control, such as market conditions, lack of market infrastructure, legislative restrictions and, in some cases, the lack of a mandate.[64]
- As previously indicated, **the geographic concentration of EREM is partly driven by differences in the development and sophistication of the markets (SIA and LFI)**. For new products such as the SIA and the LFI, the EIF adopted a deliberate and justifiable strategy of initially focusing on countries where the asset class already existed (to build champions and the EIF's own track record and experience), and then diversifying to newer markets (market-building role). Additionally, **the take-up of products such as the LFI and ABS Credit Enhancement was limited by legislative restrictions**. The SME Initiative, by contrast, suffered from the wait-and-see approach adopted by several managing authorities. There was limited take-up of the CBSI Instrument in countries with the highest SME financing needs. This was due to eligibility constraints which hampered the deployment of the product and to delays in setting up the product which constrained marketing.

[64] For instance, the EIF did not have a mandate for ESIF in Latvia.

EREM effectiveness in diversifying non-bank sources of finance for SMEs, small mid-caps and social enterprises

- **EREM resources enabled the EIF to play a key role in developing the lower mid-market segment of the European private debt industry (fund size < €1 billion) and the impact investment market.** The EIF has contributed to widening and diversifying the investor base in the lower mid-market segment of the European private debt industry and the impact investment space by attracting new classes of investors to these asset classes. In the private debt sector the EIF has pulled in institutional investors, public sector investors and high-net-worth individuals. In the impact investment space, there is evidence that the EIF's presence catalysed investment from family offices, particularly smaller ones.
- **The EIF has also contributed to developing these markets through methods outside investment, such as building new intermediaries by supporting first-time teams and strengthening intermediary capacity by providing structuring support**. The structuring input provided by the EIF was appreciated by fund managers and resulted in positive changes.
- **The lower mid-market segment of the EU private debt industry has proven to be a viable alternative channel to bank financing** by supporting both diversified loan funds (already ongoing under the Private Credit Programme of EFSI's SME Window) and selective loan funds (currently stalled). There is a strong case for the EIF to continue nurturing the development of this segment, based on both market pull factors (this evaluation found strong demand for the LFI) and push factors (potential adverse effects on levels of bank financing to SMEs due to future regulatory changes, such as the introduction of Basel IV by 2023).
- **The SIA has played a key role in establishing and promoting industry standards and best practice** in the areas of social impact measurement and reporting, and of impact-based carry. However, the impact-based carry mechanism is not perceived as having influenced the social impact delivered by assisted funds. Its main added value has been to help maintain focus on social impact and to strengthen monitoring.

EREM efficiency of implementation

- **The internal factors delaying the launch of EREM products were avoidable.** The launch and deployment of several EREM products were delayed for various internal and external reasons. Internal factors included lengthy internal discussions between the EIB and the EIF regarding the delivery model for the CBSI product, the length of time taken to approve transactions and sign agreements with financial intermediaries (SIA), and the processes involved in budget reallocations (LFI). External factors included the length of time taken for fundraising (LFI) and the wait-and-see approach adopted by managing authorities (SME Initiative). While the external factors were outside the control of the EIB and the EIF, the internal processes could have been organised more efficiently.
- **The partial delegation model adopted for the CBSI Instrument was less efficient than the full delegation model adopted for other products.** The partial delegation model of the CBSI Instrument created several operational challenges and inefficiencies, such as amendments to EIF product documentation in line with the EIB's requirements, manual double entry of transaction data on EIB systems by EIF staff, and the need to duplicate documents and processes to meet the 95:5 capital split requirement.
- For the SIA, **topping up an existing pilot product with EREM funding helped to reduce time to market** as processes, procedures and a potential pipeline of deals were already in place.
- Despite budget shifts to relatively high capital-intensive products, the **overall capital consumption of EREM was within set limits,** primarily due to the availability of external ratings for some transactions.

7.2 Evaluation recommendations

With respect to the above conclusions of the evaluation, the following recommendations are provided to the EIF and EIB services:

Recommendation 1:

When designing a mandate, the EIB should:

- Clearly specify the weight assigned to each policy objective if the mandate has more than one. To the extent possible, objective setting should be guided by a SMART[65] framework, clearly defining what success looks like. SMART objectives provide greater focus and a clearer framework for monitoring performance and ensuring accountability.
- Set objectives that are results-based rather than output-focused to ensure flexibility to respond to changes in the context.
- Ensure that the choice of products and budget allocation are aligned with the mandate's hierarchy of objectives. For example, if the objective of an intervention is to quickly get money flowing into the real economy, then it should include a limited number of simple, tried-and-tested, quick-disbursing products, rather than a complex design featuring several new and untested products.

Recommendation 2:

The EIB should explicitly set out time-to-market targets for anti-crisis instruments or instruments addressing urgent policy priorities to ensure the timeliness of its response. Accordingly, the governance arrangements and operational processes for the instrument should be designed to facilitate delivery of financing within the established timescales.

Recommendation 3:

Provided relevant mandators' resources are made available, the EIF should continue nurturing the development of the lower mid-market segment of the EU private debt industry, which has proven to be a viable alternative channel to bank financing, by supporting both diversified loan funds (already ongoing under the Private Credit Programme of EFSI's SME Window) and selective loan funds (currently stalled). There is a strong case for this based on market pull factors (this evaluation found strong demand for the LFI) and push factors (potential adverse effects on levels of bank financing to SMEs due to future regulatory changes, such as the introduction of Basel IV by 2023). If backed by relevant mandators (the EIB, the Commission and MS), future interventions should consider placing greater focus on countries which have only recently implemented a legislative framework for loan fund activity and on countries which have previously not benefited from EIF support. The EIF should consider gradually phasing out interventions in countries where private debt markets are more mature (to avoid market distortion), unless such interventions have a strong rationale (e.g. pan-European platforms) and provided mandators' terms (e.g. as regards sustainability of the mandate) allow for this.

Recommendation 4:

The EIF should intensify its marketing and capacity-building efforts to promote take-up of its products in MS where they are most needed. Although geographical take-up of products can be constrained by their demand-driven nature and lack of market infrastructure, where the EIF is entrusted with pan-European mandates, it is important to ensure that EIF support reaches the MS that need it most.

65 Specific, measurable, achievable, relevant and time-bound.

Recommendation 5:

Where within its control, the EIF should reduce the time required from the approval of a transaction to contracting. This time has varied significantly between transactions for some EREM products (e.g. SIA) and was often longer than expected. If feasible, some streamlining of procedures and strengthening of legal capacity by the EIF may help to improve efficiency.

Annex 1 – Methodology

This annex provides more details on:
- The methods and data sources used to respond to each evaluation question;
- The sampling approach and response rates of the four surveys conducted.

Methods for data collection and analysis

To respond to the evaluation questions, a **mixed methods approach** was applied. The evaluation combined a series of quantitative and qualitative analyses and drew on various data sources and analytical tools, including secondary data analysis, documentary review of EREM-specific documentation, policy and portfolio review, and surveys of and interviews with relevant stakeholders.

Table 7. summarises the main sources and methods used to respond to each of the six evaluation questions.

Table 7. Summary of methods and sources per evaluation question (EQ)

	Evaluation questions					
	Relevance		**Effectiveness**			**Efficiency**
	EQ1	**EQ2**	**EQ3**	**EQ4**	**EQ5**	**EQ6**
	Initial design	**Changes**	**Access to finance**	**Market impact**	**Social impact**	**Efficiency**
Secondary data analysis and literature review:						
• ECB SAFE survey	✓	✓				
• EIB and EIF research publications (e.g. European Small Business Finance Outlook)	✓	✓				
• EIB Investment Survey	✓	✓				
• National data on access to finance	✓	✓				
• Benchmark data from EIB mandate management team						✓
• Social investment market reports 2012-2018				✓		
• Commission social enterprise mapping reports	✓	✓				
• Relevant academic and grey material	✓	✓				
• National research and policy publications	✓	✓				
• Investment press releases and media				✓		
• Evaluations of other EIF mandates	✓	✓				✓
• Intermediary lending and investment data (company websites)			✓			
Review of EREM-specific documentation:						
• EREM Framework Agreement and instrument agreements (market assessments, business plans)	✓	✓	✓	✓		✓

• Minutes of meetings of the High-Level Steering Panel and EREM Task Force	✓	✓				✓
• EREM implementation reports	✓	✓				✓
• Operation-level documentation (for all transactions of the three instruments)			✓	✓	✓	✓
• EIF monitoring data			✓	✓	✓	
• Documents describing the EIF's due diligence process						✓
• Evaluations of SIA-backed investments (if available)					✓	
• Documentation on delivery of structuring input				✓		
Interviews:						
• EIB and EIF staff	✓	✓	✓	✓	✓	✓
• Intermediaries receiving EREM support	✓	✓	✓	✓	✓	✓
• Intermediaries not supported by EREM	✓	✓		✓		✓
• Other market players (e.g. investors)	✓	✓		✓		✓
Surveys:						
• Intermediaries (SIA, LFI and CBSI Instrument)	✓	✓	✓	✓	✓	✓
• Final beneficiaries (SIA)			✓		✓	
Contribution analysis			✓	✓	✓	

Source: EV

Secondary data were collected at three different levels: Mandate, products and transactions.

Mandate-level research included a review of all official documentation relating to the Mandate set-up and implementation, such as the:

- EREM Framework Agreement;
- Documentation presented to the MC (e.g. requests for budget reallocations);
- Requests for approval submitted to the BoD and the EIF Board;
- EIF reports on the implementation of the Mandate;
- Mid-term review and closure reports.

Product-level research included a review of:

- Product-level agreements signed between the EIB and the EIF;
- Product-specific reporting by the EIF (e.g. quarterly and annual reports);
- Academic and grey literature to inform understanding of the evolution of specific markets (private debt markets, impact investment markets and financing via cooperative banks) during the evaluation period.

Finally, transaction-level documentation was reviewed for all transactions financed under the SIA, the LFI and the CBSI Instrument. This included the following:

- Due diligence reports;
- Independent opinions;
- Requests for approval;
- Agreements and side letters;
- Contracts between the EIF and financial intermediaries, as well as any amendments;
- Monitoring reports submitted by financial intermediaries;
- Other documentation available on the websites of financial intermediaries.

Primary data collection entailed two surveys and a series of interviews with relevant stakeholders.

Two **surveys** were conducted online, targeting the following groups:

- *All financial intermediaries under the SIA (12), the LFI (17) and the CBSI Instrument (15)*. For each product, a short and focused survey was designed to explore the impact of EREM support on the financing activities of financial intermediaries, as well as their mission, investment/lending strategy, due diligence procedures and governance arrangements.
- *SIA final beneficiaries*. Because all fund managers have published the details of supported social enterprises on their websites, the contact details of final beneficiaries were easily gathered from public sources. The survey included questions to determine if social enterprises would have been able to secure financing from alternative sources had they not received investment from the SIA-backed fund, and also covered the nature of the social impact delivered and impact measurement practices.

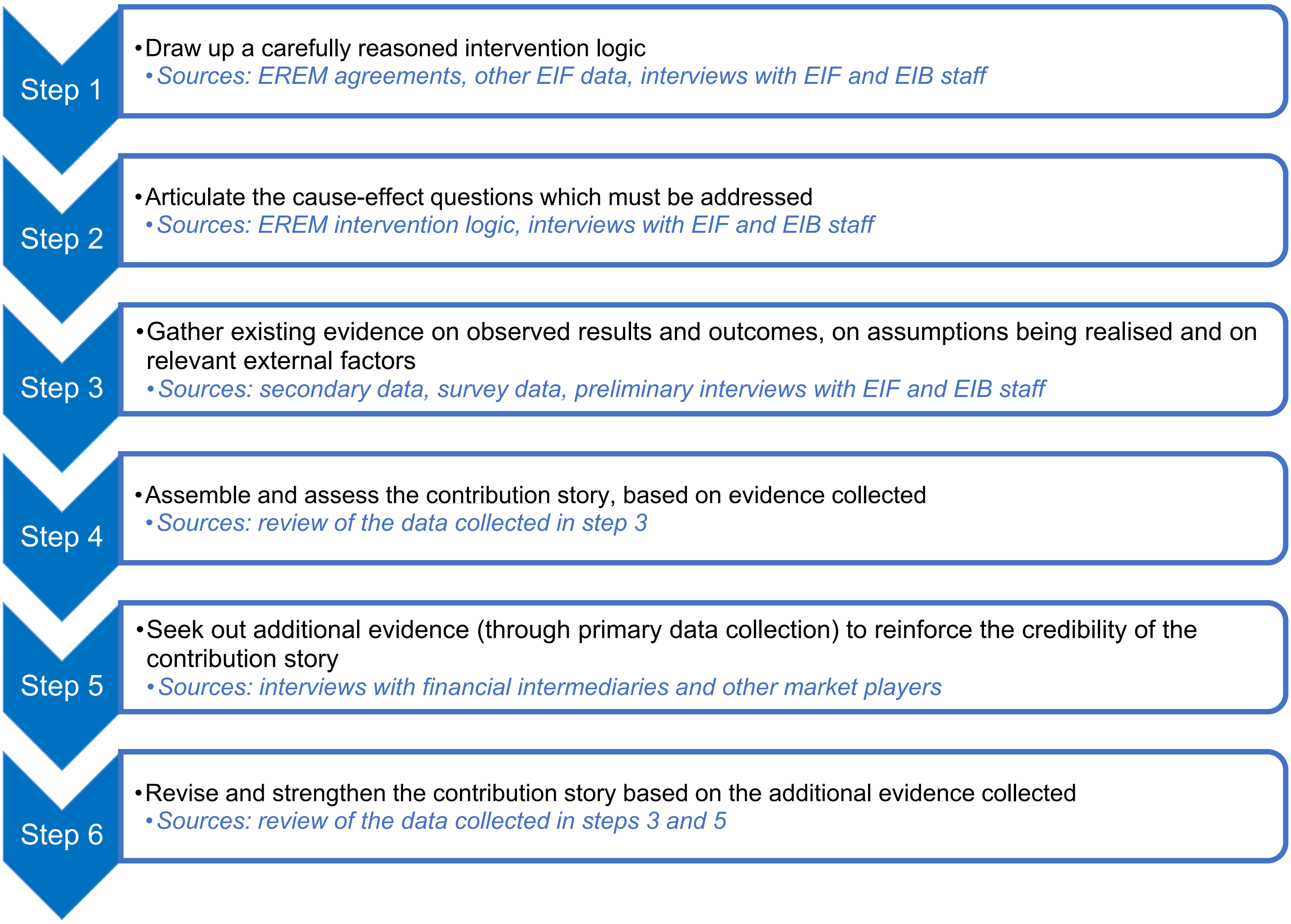
The steps involved in the survey process were as follows: (i) assembly of contacts database; (ii) questionnaire design; (iii) piloting and testing of survey; (iv) full-scale roll-out; and (v) data cleaning and analysis.

Face-to-face interviews were carried out with 15 intermediaries supported by EREM. These interviews were semi-structured and sought to explore the relevance, efficiency and effectiveness of the three EREM instruments in more detail. They served as an important source of information for the 15 case-based contribution analyses conducted by the evaluation team. The interviews complemented the quantitative data collected via the surveys (see above) and the secondary data analysis. They were held afterwards to allow the evaluation team to explore the reasons behind survey responses, to test preliminary findings from the secondary data analysis, and to better understand the impact of the three EREM instruments on respective intermediaries.

Complementary interviews were held face to face or on the phone with EIB and EIF staff (e.g. EIF relationship managers for all 15 transactions under review) and on the phone with eight other market operators (intermediaries not supported by EREM and other investors in EREM-backed impact funds or loan funds).

Case-based contribution analysis was conducted for 15 financial intermediaries. This method was used to respond to the cause-effect evaluation questions (EQ3 and EQ4). The contribution analysis sought to demonstrate a plausible association between the three EREM instruments and observed outcomes, using the weight of evidence collected through a range of sources. It was specifically used to test the key assumptions underpinning the theories of change of the three EREM instruments. The main steps of the contribution analysis are outlined in Figure 31.

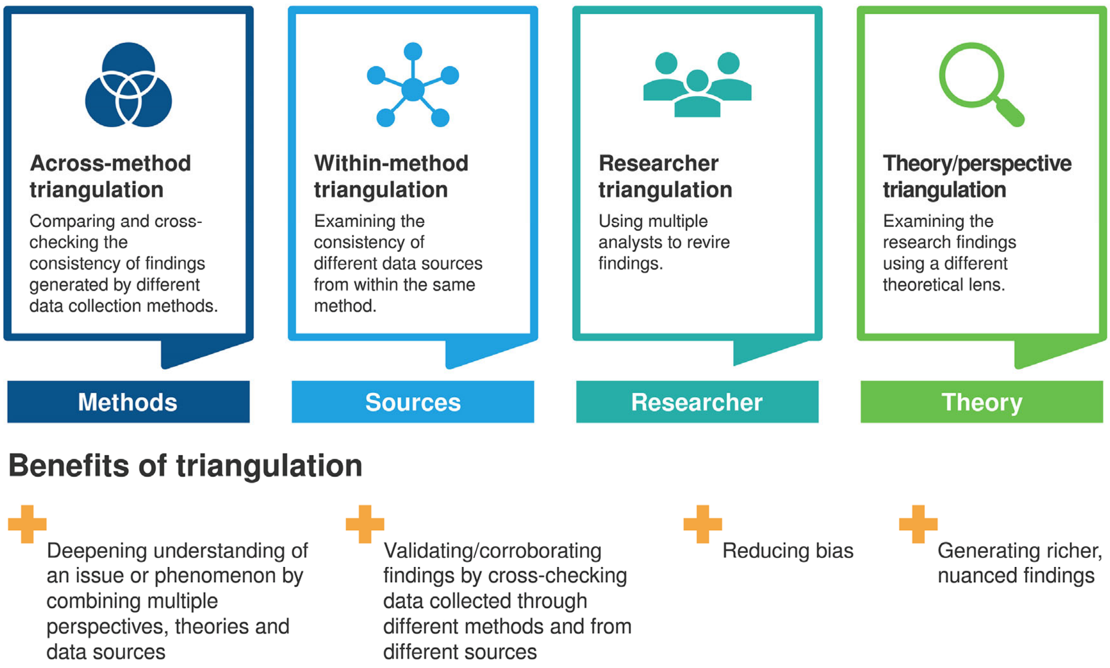
Figure 31. Steps of the contribution analysis



Source: Mayne, J., Contribution analysis: addressing cause and effect, 2011

Data collected through the above methods and sources were triangulated, as illustrated in Figure 32.

Figure 32. Approach to triangulation



Source: ICF

Approach to sampling

The following samples were used:

- *For the three surveys of financial intermediaries (for the SIA, the LFI and the CBSI Instrument),* the entire population of intermediaries was covered.
- *For the survey of SIA-backed social enterprises,* 101 social enterprises were sampled out of the total population of 141. Forty social enterprises were excluded from the sample for one of the following reasons:
  - The loan/investment date was in 2019, which is outside the scope of this evaluation.
  - The type of instrument used by the fund was not suitable for the survey. One fund uses social bonds which apply a complex structure of stakeholders, and many of the survey questions were simply not applicable to this context.
  - The type of businesses supported by the fund was not suitable for the survey. One fund was similar to a debt fund providing small loans to franchises in disadvantaged regions. What made those companies social enterprises was their focus on disadvantaged areas, and not their business model. Therefore, a number of questions included in the survey were not directly applicable to them.
  - The company no longer existed when the survey was launched.
- *For the face-to-face interviews with supported intermediaries*, a relatively small sample size (15) was chosen because the surveys of financial intermediaries had high response rates and revealed relatively low divergence of opinions. The sample covered all three instruments central to the scope of the evaluation and was designed in a purposeful manner. It was intended to capture: (i) different country contexts; (ii) different profiles of

intermediaries; and (iii) the diverse views expressed in the online surveys. The final sample was adjusted based on practical considerations.

- *For the phone interviews with non-supported intermediaries and with investors who invested alongside the EIF or other wholesale investors*, contact details were gathered from public sources, focusing on those countries where the site visits took place. The evaluation targeted a sample of 40 organisations. Unfortunately, only eight agreed to participate in a phone interview.

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Annex 3 – EREM background and theories of change

In mid-2013, against the background of a weak short-term economic outlook and high youth unemployment, the European Council[66] urged immediate action and called for the mobilisation of European resources, including those of the EIB Group, to leverage private sector and capital market instruments to benefit SMEs. Furthermore, it welcomed the increase in the EIF's credit enhancement capacity alongside (and very complementary to) the large equity mandate (Risk Capital Resources). At that time, the EIF management deemed that the EIF's capital base precluded any significant expansion of its activities. Concurrently, within the context of the Multiannual Financial Framework 2014-2020, the EIB Group and the European Commission discussed reinforcing the EIF's role as a countercyclical entity.

To answer the European Council's call and address the EIF's challenges, the October 2013 meeting of the BoD discussed the possible EIF capital increase and the establishment of the EIB Group Risk Enhancement Mandate (EREM) to be managed by the EIF on EIB Group risk. On 16 and 17 December 2013, the EIF Board and the BoD, respectively, approved €6 billion for EREM with a view to increasing the EIF's capacity to support SMEs' access to finance and to complementing the EIF's capital increase in 2014. Both decisions showed a clear response by the EIB Group to the European Council's 2013 request.

The overarching objective of EREM was to increase access to finance for SMEs and small mid-caps by strengthening the credit enhancement capacities of the EIF and by delivering finance mainly through financial institutions, including guarantee institutions.

Main policy documents delineating EREM objectives

While it was not until mid-2013 that EU leaders – gathered at the European Council meeting of 28 June 2013 – expressly recognised the need to reinforce the EIF's credit enhancement capacity, the origins of EREM and the identification of its target issue (SME financing constraints) can be traced back to:

- The 2008 Small Business Act for Europe – the overarching EU policy framework for SMEs – which was subject to a review in 2011 and a public consultation in 2014;
- The Compact for Growth and Jobs, which was announced by the European Council in mid-2012;
- The proposals for the Multiannual Financial Framework 2014-2020 tabled by the Commission in mid-2011, which revealed a preference for using financial instruments (rather than grants), and hence spotlighted the important role of the EIF in mobilising public and private funding;
- The flagship SME Initiative as a potentially pan-European scheme.

Since the EIF's inception in 1994, SME financing and, more generally, the achievement of EU policy objectives have been core to the EIF's mission and enshrined in its statutory requirements. Signed on 14 March 2014, EREM was the first of two measures that year to reinforce the EIF's credit enhancement capacity. The other measure was the EIF's capital increase, which followed just a few months later in mid-2014.

Overview of the instruments and activities under EREM

The EREM Framework Agreement envisaged at least eight instruments. Only six of these were ultimately signed and implemented:

- <u>*Social Impact Finance (SIF) contributing to the Social Impact Accelerator (SIA)*</u>

EREM funds allocated to the SIF increased the EIF's commitment to an existing initiative – the SIA – originally financed by the EIB under the Risk Capital Resources Mandate, with

[66] European Council, Conclusions – 27-28 June 2013.

commitments from other entities and the EIF's own resources. Under this instrument, the EIF invests (equity) in social impact funds which support social enterprises. The SIA aims at pioneering social impact investing and contributing to the creation of sustainable funding market infrastructure for social entrepreneurship in Europe.

- *Asset-Backed Securities (ABS) Credit Enhancement Instrument*

Under this instrument, the EIF provides guarantees in the context of securitisation,[67] mainly for unfunded (synthetic) or funded (true sale) transactions[68], primarily to increase the ticket size and broaden the scope of EIB Group ABS-related activities, from AAA (senior) to BB (mezzanine).[69] The aim is to provide capital relief to financial intermediaries (known as originators). On the back of this support, financial intermediaries commit to generating an additional portfolio of loans to SMEs and small mid-caps, as a multiple of the amount of the tranche guaranteed by the EIF.

- *Loan Funds Instrument (LFI)*

Under this instrument, the EIF makes equity investments in funds that lend to SMEs and small mid-caps. As a result of the global financial crisis and the additional regulatory requirements that followed, traditional banks face several constraints in terms of lending to counterparties perceived to be higher risk, such as SMEs and small mid-caps. This instrument aims at widening the availability of non-bank financing to SMEs and small mid-caps, notably through investment funds, whose regulatory burdens remain lighter. The LFI envisaged both selective loan funds (non-granular portfolio) and diversified loan funds (granular portfolio).[70]

- *Cooperative Banks and Smaller Institutions (CBSI) Instrument*

Under this instrument, the EIF lends to eligible cooperative banks and smaller financial institutions, which on-lend to SMEs and small mid-caps. The purpose of the CBSI Instrument was to contribute to widening the availability of small bank and non-bank loans for SMEs and small mid-caps, beyond traditional bank financing. The EIB Group did not previously finance this group of financial intermediaries due to their small ticket size or low credit rating.

- *SME Initiative (Option 1 and 2)*

Under this instrument, a number of risk-takers mandate the EIF to provide guarantees on their behalf to financial intermediaries which lend to SMEs. The risk-takers are the following, in ascending order of seniority:

- European Structural and Investment Funds (ESIF) – first-loss or junior tranche of the MS or managing authorities opting in to the initiative;
- European Union (COSME and Horizon 2020) – second-loss or lower mezzanine tranche;
- EIB and EIF, through EREM – upper mezzanine tranche;
- EIB and/or EIF, with their own resources – senior tranche.

The SME Initiative has two products: Option 1 – portfolio guarantee; and Option 2 – guarantee in the context of securitisation. The final aim under both options is to support financial intermediaries in generating a portfolio of loans to SMEs corresponding to a minimum multiple of the ESIF amount contributed by the MS or managing authorities opting in to the initiative. It was expected that by joining forces in this way, the SME Initiative would achieve economies of scale and create greater added value compared to the alternative scenario of funds being deployed under separate initiatives. Without the SME Initiative, ESIF funding would have typically been used as grants (i.e. one-off subsidy payments). However, for those MS willing to adhere to the SME Initiative, ESIF

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67 Securitisation is the process of taking an illiquid group of assets, in this case a portfolio of lending to SMEs and small mid-caps, and through financial engineering, transforming them into a security. Hence the term "securitisation".

68 There are two main types of securitisation: cash (funded or true sale) and synthetic (unfunded).

69 Risk tranching is a financial engineering technique applied in securitisation whereby securities are divided according to risk characteristic to be marketable to different investors. Typically we will have senior, mezzanine and junior tranches with low, moderate and high risk, respectively.

70 A granular portfolio is well diversified across a wide variety of areas, typically with a significant number (a good proxy would be > 100) of underlying risk counterparties.

funding could instead be used as a first-loss piece for other more senior credit risk protection providers, as described above.

The EIF did not implement the following two instruments initially envisaged in the EREM Framework Agreement[71]:

- *Youth Employment Programme (YEP)*

Under this instrument, the EIF would have provided partial guarantees for commercial loans to SMEs and small mid-caps which created jobs and offered apprenticeships to young people. The aim of the proposed YEP was to support youth employment in Europe by building a link between the EIB Group's financing and the employment of young people. The instrument was not implemented due to a lack of first-loss protection.

- *Microfinance Instrument*

Under this instrument, the EIF would have funded microfinance intermediaries. This instrument initially envisaged under EREM was subsequently developed under the EU-funded Employment and Social Innovation (EaSI) programme.

EREM budget

The above-mentioned EREM instruments were to be deployed over a seven-year timeframe (2014-2020) with an overall investment capacity of up to €6 billion. This was to be split two-thirds to one-third between the EIB and the EIF on an overall nominal basis. This means that the split did not have to materialise for each individual transaction or instrument but for the whole EREM. Joint EREM commitments to the instruments were expected to total up to €3.4 billion during the 2014-2016 period (first period). On 28 April 2017, the BoD approved a one-year extension of the first period of EREM approvals, up to 31 December 2017.

The specific budgetary allocations were initially based on each instrument's expected market demand and time to market delivery, as well as the desire of the EIB's Risk Management Directorate to properly monitor the capital consumption of EREM (not to exceed 0.5% of the EIB's capital adequacy ratio (CAR)). The EIB's first tranche amount was set at €2.3 billion. Finally, as explained above, only six instruments were signed: neither the YEP nor the Microfinance Instrument materialised. Likewise, the Risk-Sharing Instrument, which despite not being listed in the EREM Framework Agreement was initially allocated a small budget, did not materialise either due to lack of EIB or third-party protection. The same applied for the YEP.

Because the initial budgetary split across instruments did not correspond to the actual market demand experienced during the first period, several budgetary reallocations were carried out, with funds transiting as follows:

- First from the SME Initiative to the LFI (€550 million) and the ABS Credit Enhancement Instrument (€125 million);
- Later from the SME Initiative Option 1 to Option 2 (€250 million) and from the SME Initiative Option 1 and the ABS Credit Enhancement Instrument to the LFI (€327.8 million).

[71] Moreover, between the signature of the EREM Framework Agreement and the initial allocation of the budget, the EIF temporarily envisaged but did not implement a product based on the Risk-Sharing Instrument model, supporting a dedicated guarantee programme using EIB or third-party funds as first-loss protection.

Table 8 presents the initial budgets of the different EREM instruments, the initial first period budgetary split and the final first period split.

Table 8. EREM budget

EREM Instruments	Initial Investment Capacity Allocation € m				Initial EREM Budget (First Period) € m				Final EREM Budget after reallocations (First Period) € m			
	Total	% of EREM Total	EIB	EIF	Total	% of EREM Total	EIB	EIF	Total	% of EREM Total	EIB	EIF
EREM ABS Credit Enhancement	1 950	33%	67%	33%	890	30%	67%	33%	855	31%	67%	33%
EREM SME Initiative (Option 1)	1 500	25%	67%	33%	1 310	45%	67%	33%	245	9%	42%	58%
EREM SME Initiative (Option 2)	300	5%	67%	33%	250	9%	67%	33%	250	9%	67%	33%
EREM Loan Funds	525	9%	95%	5%	175	6%	95%	5%	1 053	38%	95%	5%
EREM Microfinance	105	2%	95%	5%	-		-	-	-		-	-
EREM CBSI Instrument	600	11%	95%	5%	125	4%	95%	5%	195	7%	95%	5%
EREM Youth Employment	425	7%	0%	100%	-		-	-	-		-	-
EREM Social Impact Finance	315	5%	95%	5%	189	6%	95%	5%	189	7%	95%	5%
Other Risk Sharing Instrument type	250	4%	0%	100%	-		0%	0%	-		-	-
EREM Total	**6 000**	**100%**	**67%**	**33%**	**2 939**	**100%**	**71%**	**29%**	**2 787**	**100%**	**79%**	**21%**

Source: EIF

EREM governance

The EREM Framework Agreement envisaged full delegation.[72] However, in practice, some of the instruments involved partial delegation. For instance, loan administration for the CBSI Instrument was carried out by the EIB. EREM was based on strict sharing of information and decisions between the EIB and the EIF, within the provisions of the Mandate and instrument agreements. At the same time, EREM envisaged overall co-investment from the EIB and the EIF. To ensure a coherent intermediated finance offer and client relationship management, the two Group entities agreed upon detailed collaboration and coordination guidelines (Article 3, EREM Framework Agreement).

The overarching principles for EREM collaboration and implementation were:

- Complementarity with EIB and EIF products: there should be no overlap or crowding-out of existing EIB Group offers;
- Efficient leverage of EIF expertise, products, systems and procedures, particularly in the areas of assessing and structuring granular portfolios;
- Coordination and cooperation between the EIB and the EIF aimed at:
  - Coherent risk management across the Group;
  - Coherent client relationship management across the Group, especially for common transactions where the EIB already had a relationship with the counterparty.

The following bodies have collaboration and coordination responsibilities for EREM activities:

- High-Level Steering Panel;
- EREM Task Force;
- EIB Ops Geographical Departments and/or global relationship managers and the EIF equivalents.

[72] Under the EREM Framework Agreement, the EIB delegates to the EIF the origination, due diligence, structuring, monitoring, servicing, work-outs as well as pricing and rating of the underlying transactions. For a number of EREM instruments, the EIB retained a non-objection right, yet generally only EIF Board approval is sought for the approval of a new transaction.

For each of these bodies, Table 9 describes their tasks, composition and meeting frequency.

Table 9. EREM's governance, collaboration and coordination

Structure	High-Level Steering Panel	EREM Task Force	EIB Group Front Offices
Tasks	Reviewing and providing guidance regarding EREM and its implementation	Coordinating the implementation of the Mandate, entailing secretarial support to EREM coordination meetings, providing information and preparing the agenda for the High-Level Steering Panel meetings, analysing the online pipeline, reviewing implementation progress, monitoring the CAR impact, being the main point of contact for EREM for internal and external counterparties, etc.	Coordinating between the EIB and the EIF on counterparty selection, marketing, transaction origination and overall client relationship management
Composition	Representatives from the EIB and the EIF	EREM coordinators appointed by the EIF and the EIB	EIB group relationship managers and EIF equivalents
Meetings	At least twice per year during the implementation period	Tentatively on a monthly basis and no less than six times per year during the implementation period	No meetings

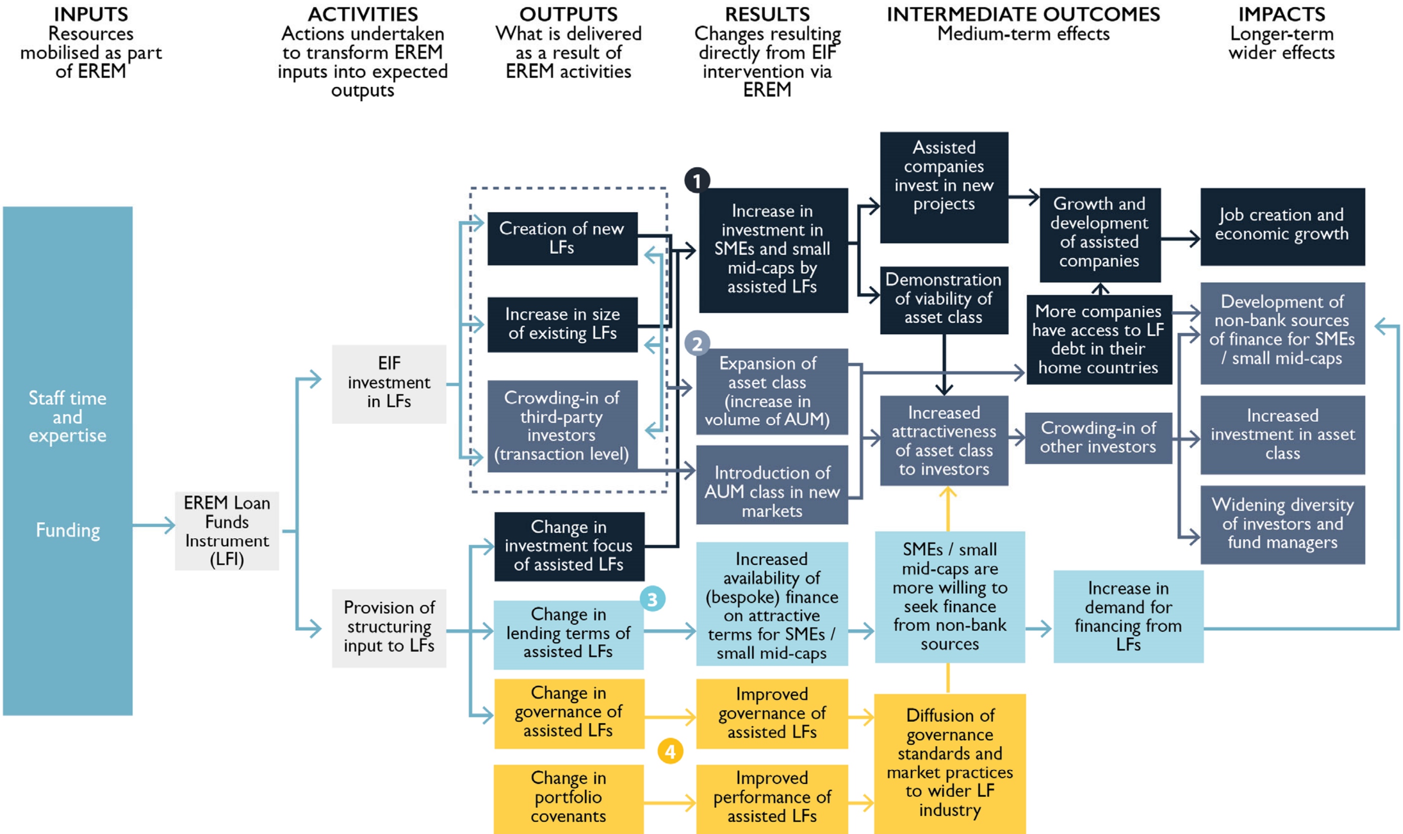
Source: EV, adapted from the EREM Framework Agreement

Moreover, coordination efforts included the EIF sharing the pipeline of potential operations relating to each instrument with the EIB, as set out in Article 3.5 of the EREM Framework Agreement.

EREM entailed coordination at different levels:

- Instrument development, implementation and pricing: the EIF shall lead on these matters; notably, pricing should follow the EIF's principles with disclosure to the relevant EIB services;
- Business planning: MC approval is required to start implementation of any instrument under EREM; EREM instrument proposals by EREM coordinators should be accompanied by a market assessment, origination strategy and business plan, enabling the EIB to assess volumes and the impact on the CAR;
- Counterparty selection, marketing, transaction origination and overall client relationship management:
    - EIB Ops Geographical Departments and/or global relationship managers and the EIF equivalents shall have the lead relationship with counterparties within their geographic remit, and set priorities considering the targets of the EIF's Corporate Operational Plan;
    - The EIF shall engage in marketing activities for EREM in specific countries, in coordination with EIB Ops Geographical Departments;
- Transaction approval:
    - For all transactions proposed under EREM, approval by the EIF Board must be in accordance with the EIF's customary procedures;
    - For all shared transactions – i.e. those entailing an EIB commitment outside EREM coupled with EREM intervention – the EIB's non-EREM financing has to be approved by the BoD. Presentations aimed at transaction approval by the respective Boards have to be coordinated;
    - Collaboration and coordination is based on a principle of non-objection by the EIB. Any decision under Annex 4 of the EREM Framework Agreement shall be deemed to have the EIB's consent if the EIB has not objected in writing (including by email) to the EIF's proposal within seven business days.

Figure 33. Theory of change for the LFI



Source: EV

The theory of change (ToC) for the LFI maps out the different components of the instrument (investment, structuring input) and identifies a conceptual and logical progression of the changes the instrument aims to influence if it is to be successful. The ToC is a conceptual model, not a literal representation of a linear process.

It depicts the investments and activities of the LFI, namely investments in selective and diversified loan funds and the provision of structuring input to selected loan funds. These investments and activities are expected to produce a set of outputs that include (i) mobilisation of investment from other sources; (ii) creation of new funds or increase in the size (and thus lending capacity) of existing loan funds; and (iii) changes to the fund's investment strategy, characteristics of financial products, team composition and reporting based on the structuring input provided by the EIF.

These outputs are, in turn, expected to lead to a series of short-term, intermediate and longer-term changes. The short-term changes are directly within EREM's sphere of influence and include the increased capacity of loan funds to lend to SMEs and small mid-caps (as a result of EIF investment and the other investment it catalyses), greater focus on SMEs and small mid-caps, developing more suitable financial products for them (in terms of loan values, terms or return expectations), and changes to fund governance (e.g. independence and remuneration of fund managers, improved reporting to investors).

If these short-term changes are achieved, the ToC identifies four pathways of change through which the intermediate and longer-term changes are likely to follow:

Pathway 1: The increased capacity of funds (together with an increased focus on and more appropriate products for SMEs and small mid-caps) results in increased lending to SMEs and small mid-caps at intermediary and market levels (overall increase in volumes, expansion in availability of debt from loan funds in MS that had not been introduced to this new asset class). SMEs and small mid-caps thus benefit from a diverse choice of direct lending funds offering flexible debt structures in a greater number of countries. The debt accessed from loan funds is invested by companies in projects that contribute to their growth and development.

Achievement of this pathway rests on the following assumptions:

- Funds selected by the EIF are relevant and appropriate;
- The EIF's presence has a signalling effect for other investors;
- In the absence of EIF investment via EREM, the assisted loan funds would not be established or would be set up on a smaller scale;
- There is demand for financing from debt/loan funds among SMEs and small mid-caps;
- Loan funds offer financing on attractive terms to SMEs and small mid-caps.

Pathway 2: The EIF's intervention contributes to developing the loan fund industry (particularly in underserved countries) targeting SMEs and small mid-caps by increasing the number and size of funds, attracting new and diverse investors. This, in turn, contributes to developing non-bank sources of finance for SMEs.

Underlying assumptions:

- The EIF's presence has a signalling effect for other investors;
- In the absence of EIF investment via EREM, the assisted loan funds would not be established or would be set up on a smaller scale;
- The assisted funds are viable.

Pathway 3: The availability of finance on flexible and attractive terms (from a locally based loan fund) creates demand for the product, thus supporting the development of the asset class.

Underlying assumptions:

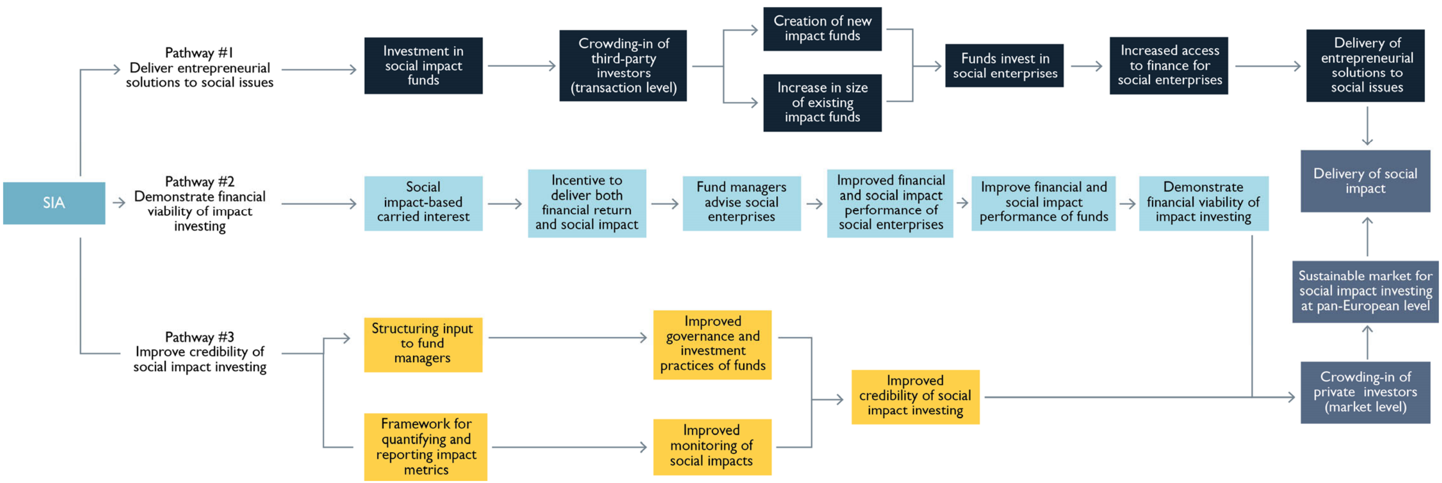
- There is demand for financing from debt/loan funds among SMEs and small mid-caps;
- The assisted funds are viable;
- Loan funds offer financing on attractive terms to SMEs and small mid-caps.

Pathway 4: When supporting new funds as a cornerstone investor, the EIF offers fund managers advice on market best practices and governance, analysing the underlying portfolio and encouraging the fund to implement portfolio covenants to improve the fund's risk-return profile. This helps to improve the performance of the assisted fund. Furthermore, changes to fund governance help to improve the overall governance structure of the fund. The improved performance and governance of funds and the wider diffusion of these practices by the loan fund industry contributes to making the asset class more attractive to investors.

Underlying assumptions:

- The structuring input (governance, covenants) provided by the EIF is regarded as good practice within the industry;
- The structuring input provided by the EIF is relevant and useful;
- The structuring input is taken up and implemented by fund managers.

Figure 34. Theory of change for the SIA



Source: EV

Pathway #1: The SIA contributes to delivering entrepreneurial solutions to social issues
The EIF intended to address a market gap by increasing the supply of capital available for investment in social enterprises. It did so by investing in social impact funds. The EIF's presence in these funds was expected to crowd in additional investors at the transaction level. The investments made by SIA-backed funds were, in turn, expected to enable social enterprises to scale up their activities and deliver entrepreneurial solutions to social issues.

Underlying assumptions:

- Fund managers are committed to achieving social impact;
- There is a lack of adequate funding for social enterprises;
- Without the SIA, funds would not have been established at all or only at a smaller scale;
- The EIF's presence has a positive signalling effect for other investors.

Pathway #2: The SIA contributes to demonstrating the financial viability of impact investing
The EIF requested the introduction of the impact-based carry mechanism in all the funds it backed. This means that fund managers are only entitled to receive the carried interest (an additional form of remuneration) if, in addition to delivering a significant financial return, they also achieve their predefined social impact targets. This was expected to incentivise fund managers to pay due attention to both financial return and social impact. Fund managers, in turn, were expected to advise and provide support to social enterprises to enable them to improve their financial and social performance. The positive financial and social performance of social enterprises translates into positive performance by the funds. This was, in turn, expected to help demonstrate the financial viability of impact investing and thereby attract other investors.

Underlying assumptions:

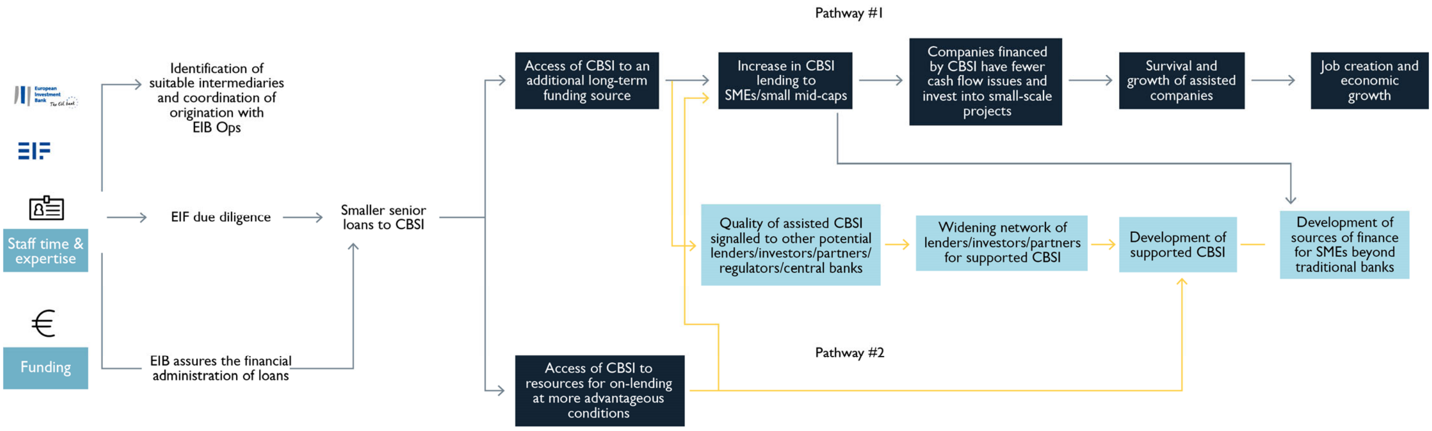
- The assisted funds will achieve a positive financial return;
- Without the impact-based carry mechanism, the social impact delivered by the enterprises would be lower;
- Fund managers have the capacity to identify and support promising social enterprises.

Pathway #3: The SIA contributes to improving the credibility of social impact investing
The structuring input provided by the EIF was intended to lead to improved governance and investment practices in the funds. The social impact measurement methodology introduced by the SIA aimed to improve monitoring of the social impact delivered by supported social enterprises. The ultimate aim of all these effects was to improve the credibility of social impact investing, thus making it more attractive to other investors.

Underlying assumptions:

- Fund managers value the EIF's structuring input and market-building activities;
- The impact measurement framework is applied in practice by fund managers;
- Social impact measurement indicators are of good quality and reliable;
- EIF-driven governance changes make funds more attractive to investors;
- The EIF's impact measurement methodology improves the credibility and attractiveness of impact investing.

Figure 35. Theory of change for the CBSI Instrument



Source: EV

Pathway #1: The CBSI Instrument results in increased lending to SMEs and small mid-caps
By providing financial intermediaries access to longer-term sources of funding, the CBSI Instrument enhances their capacity to lend to SMEs and small mid-caps. This increased lending supports SMEs and small mid-caps in meeting their working capital needs and/or making project investments, thus contributing to their sustainability and growth.

Underlying assumptions:

- The EIF has the capacity to manage the CBSI Instrument;
- In the absence of CBSI loans via EREM, lending to SMEs and small mid-caps by supported financial institutions would have been smaller or more costly;
- There is a lack of adequate debt finance for SMEs and small mid-caps;
- There is demand for debt finance by SMEs and small mid-caps from CBSI financial intermediaries.

Pathway #2: The CBSI Instrument contributes to developing supported financial intermediaries
EIF loans signal the health and profitability of CBSI financial intermediaries, improving their reputation and how they are perceived within their national and/or regional markets and among potential investors. This supports their long-term development and growth. Moreover, the CBSI Instrument provides financial intermediaries with resources at advantageous terms and conditions for on-lending, thereby improving their overall health and profitability.

Underlying assumptions:

- A relationship with the EIF has a signalling effect for other lenders, investors and/or partners of the financial institutions benefiting from the CBSI Instrument;
- EIF loans are provided to financial intermediaries on attractive terms and conditions.

Annex 4 – Supporting data

Table 10. EREM commitments (€) by Member States as of 31 December 2018 in relation to access-to-finance gaps

	EREM commitments € m	Access-to-finance gaps: EIF EASF	Access-to-finance gaps: ECB SAFE	Access-to-finance gaps: EIBIS	% Total EREM commitments	% Total EIF financing	% EU GDP	% EU SMEs
	Dec 18	2013-18	2013-18	2015-18	2014-18	2014-18	2018	2015
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
Austria	54.50	0.5	7%	18%	2.6%	2.9%	2.4%	1.4%
Belgium		0.5	9%	23%		1.6%	2.9%	2.6%
Bulgaria	34.33	0.3	10%	31%	1.6%	2.0%	0.4%	1.4%
Croatia		0.2	15%	37%		0.5%	0.3%	0.6%
Cyprus		0.1	27%	47%		0.2%	0.1%	0.2%
Czech Republic		0.4	7%	18%		2.0%	1.3%	4.2%
Denmark	13.39	0.4	11%	17%	0.6%	0.6%	1.9%	0.9%
Estonia	20.50	0.3	7%	23%	1.0%	0.1%	0.2%	0.3%
Finland	17.00	0.6	8%	19%	0.8%	1.8%	1.5%	0.9%
France	**453.50**	**0.6**	**10%**	**26%**	**21.5%**	**13.6%**	**14.8%**	**11.4%**
Germany	**239.10**	**0.6**	**7%**	**19%**	**11.3%**	**10.4%**	**21.0%**	**10.3%**
Greece		0.1	26%	66%		2.5%	1.2%	2.9%
Hungary	8.19	0.3	11%	29%	0.4%	0.6%	0.8%	2.3%
Ireland		0.3	13%	26%		1.3%	2.0%	1.1%
Italy	**465.00**	**0.3**	**12%**	**48%**	**22.0%**	**11.5%**	**11.1%**	**15.1%**
Latvia		**0.4**	**11%**	**62%**		**0.1%**	**0.2%**	**0.5%**
Lithuania	12.50	0.4	14%	36%	0.6%	0.1%	0.3%	0.8%
Luxembourg	30.00	0.5	6%	20%	1.4%	0.7%	0.4%	0.1%
Malta	16.27	0.5	9%	26%	0.8%	0.2%	0.1%	0.1%
Netherlands	**145.00**	**0.4**	**12%**	**22%**	**6.9%**	**4.5%**	**4.9%**	**4.8%**
Poland	89.16	0.4	8%	36%	4.2%	4.5%	3.1%	7.2%
Portugal		0.3	12%	35%		4.8%	1.3%	3.6%
Romania	94.38	0.2	11%	39%	4.5%	3.0%	1.3%	2.0%
Slovakia		**0.3**	**8%**	**26%**		**0.4%**	**0.6%**	**1.9%**
Slovenia		**0.4**	**15%**	**23%**		**0.1%**	**0.3%**	**0.6%**
Spain	**194.25**	**0.4**	**12%**	**50%**	**9.2%**	**17.3%**	**7.6%**	**10.9%**
Sweden	62.50	0.6	10%	12%	3.0%	2.7%	3.0%	2.9%
United Kingdom	**160.82**	**0.6**	**9%**	**18%**	**7.6%**	**10.2%**	**15.2%**	**8.8%**
EU 28	**2 110.39**	**0.4**	**10%**	**29%**	**100%**	**100%**	**100%**	**100%**

(1) Commitments as of 31 December 2018.
(2) Composite index average value over the period 2013-18.
(3) % of firms stating that "access to finance" is currently the most pressing problem they face.
(4) % of firms stating that "availability of finance" is a major obstacle PLUS % of firms that are credit constrained.
(5) EREM commitments to a particular Member State as a share of total EREM commitments.
(6) EIF financing (from all different sources) to a particular Member State as a share of total EIF financing. (Source: EIF)
(7) GDP of a particular Member State as a share of total EU GDP. (Source: Eurostat)
(8) SMEs in a Member State as a share of the total number of SMEs in the European Union. (Source: Eurostat)

Sources: EIF ESAF, ECB SAFE, EIF reporting on EREM, Eurostat

Table 11. Indicative leverage (based on EREM RfA) versus expected leverage (based on signed volumes)

	EREM budget € m	Indicative leverage as per EREM RfA	Leveraged financing – indicative* € m	Signatures as of 31 Dec 2019 € m	Leveraged financing – expected volumes** € m	Expected leverage**	Expected leveraged financing as % of indicative leveraged financing
ABS Credit Enhancement Instrument	855	10.0	8 550	855	28 000	32.8	327%
SME Initiative Option 1	245	14.7	3 602	266			
SME Initiative Option 2	250	26.7	6 675	19	223	11.5	3%
Loan Funds Instrument	1 053	4.0	4 212	781	4 785	6.1	114%
Social Impact Accelerator	189	2.5	473	176	580	3.3	123%
CBSI Instrument	195	2.0	390	152	285	1.9	73%
EREM total	**2 787**	**8.6**	**23 901**	**2 248**	**33 873**	**15.1**	**142%**

* *Calculated as follows: EREM budget x indicative leverage.*

** *Based on signed volumes. The EIF separately provided the figures for leveraged financing for the ABS Credit Enhancement Instrument and the SME Initiative Option 2 following the Emerging Findings Meeting in January 2020. Data not available for the SME Initiative Option 1. For the SIA/SIF, the LFI and the CBSI Instrument the leveraged financing is based on transaction documentation.*

Source: EV

Table 12. Average size of EREM investment per enterprise

	EREM budget € m	Leveraged financing – indicative* € m	Total number of beneficiaries **	Average amount of new loans* € m	Financing leveraged as of 31 Dec 2019 € m	Actual number of beneficiaries (31 Dec 2019)	Actual average size of investment €**
ABS Credit Enhancement Instrument	855	8 550	81 225	100 000	28 000	51 430	544 429
SME Initiative Option 1	245	3 602	34 137	100 000		53 209	
SME Initiative Option 2	250	6 675	63 333	100 000	223	1 050	212 190
Loan Funds Instrument	1 053	4 212	16 006	250 000	2 013	1 239	1 625 029
Social Impact Accelerator	189	473	451	1 000 000	154	195	788 055
CBSI Instrument	195	390	7 410	50 000	175	2 025	86 397
EREM total	**2 787**	**23 901**	**202 562**	**1 600 000**	**30 565**	**109 148**	**3 256 100**

* *Figures based on EREM RfA.*

** *Calculated by dividing the financing leveraged as of 31 Dec 2019 by the actual number of beneficiaries.*

Source: Based on data provided by the EIF

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In 1995, Operations Evaluation (EV) was established with the aim of undertaking ex-post evaluations both inside and outside the European Union. Within EV, evaluation is carried out according to established international practice, and takes account of the generally accepted criteria of relevance, efficacy, efficiency and sustainability. EV makes recommendations based on its findings from ex-post evaluation. The lessons learnt should improve operational performance, accountability and transparency. Each evaluation involves an in-depth evaluation of selected investments, the findings of which are then summarised in a synthesis report.

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OPERATIONS EVALUATION

Evaluation of the EIB Group Risk Enhancement Mandate

September 2020

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