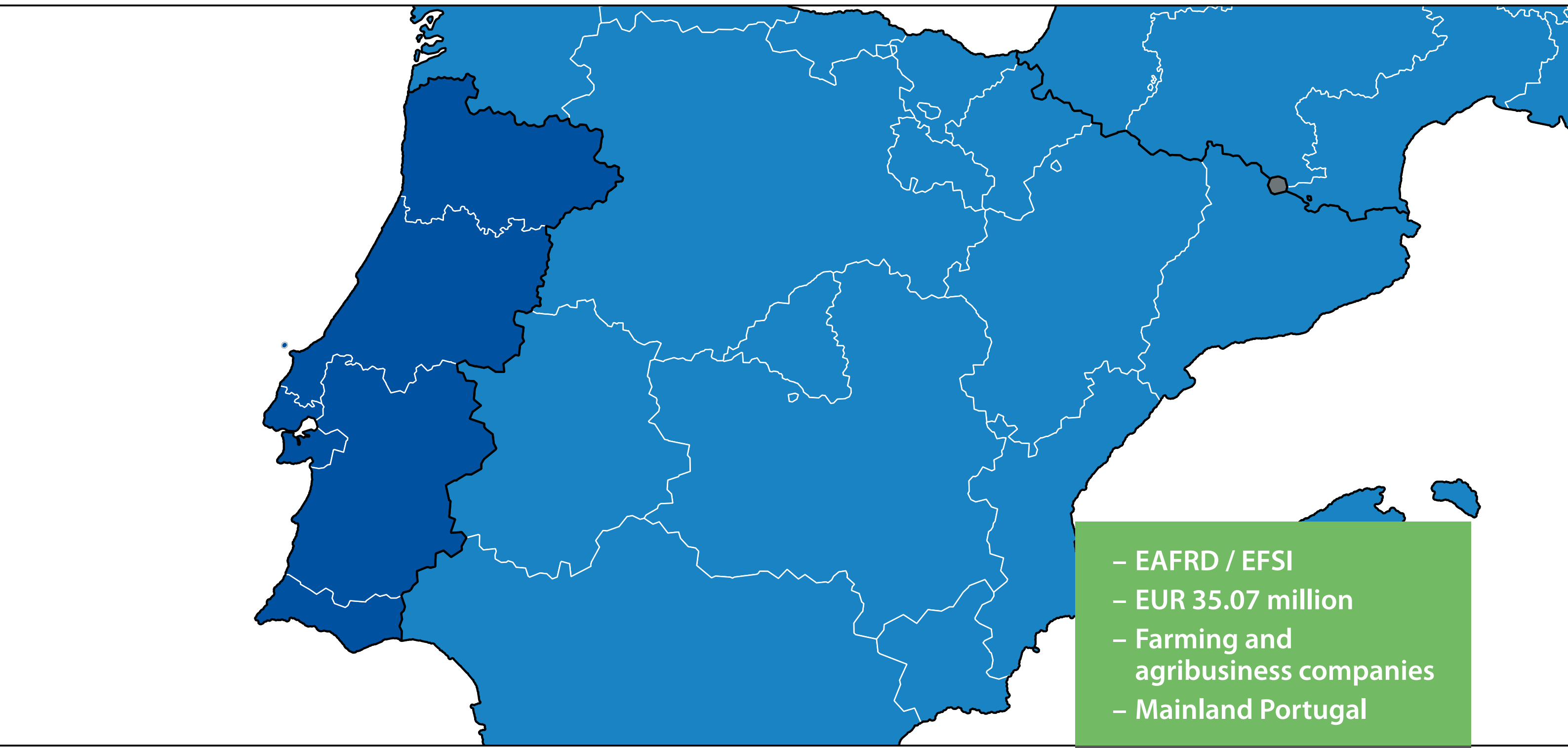

- EAFRD / EFSI
- EUR 35.07 million
- Farming and agribusiness companies
- Mainland Portugal

... providing better access to finance for final recipients in the agricultural and agri-industrial sectors...

EAFRD Guarantee Instrument 2014-2020 Portugal

Case Study

European Commission

European Investment Bank
The EU bank

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Abbreviations

Abbreviation	Full name
CPR	Common Provisions Regulation
CRII	Coronavirus Response Investment Initiative
EAFRD	European Agricultural Fund for Rural Development
EFSI	European Fund for Strategic Investment
EC	European Commission
EIB	European Investment Bank
EIF	European Investment Fund
ESI Funds	European Structural and Investment Funds
FoF	Fund of Funds
GGE	Gross Grant Equivalent
IACS	Integrated Administration and Control System
RDP	Rural Development Programme
SMEs	Small and medium-sized enterprises
TFEU	Treaty on the Functioning of the European Union

Table of contents

1. Summary

This case study presents the European Agricultural Fund for Rural Development (EAFRD) financial instrument for the Portuguese agricultural and agri-industrial sector, featuring a portfolio guarantee under a Fund of Funds (FoF) structure set up in 2019. The financial instrument is supported by the Rural Development Programme (RDP) 2014-2020 of the Portuguese Republic with a contribution of EUR 18.53 million from EAFRD and EUR 1.54 million from the national budget, plus up to EUR 15 million from the European Fund for Strategic Investment (EFSI).

As pointed out by the ex-ante assessment covering all sectors of the economy supported by ESIF, Portuguese enterprises are generally undercapitalised and heavily indebted. For agriculture, particular challenges relate to access to financing and disproportionally high financing costs compared to profitability in the sector. The banking sector tends to be reluctant to lend to farmers and agri-industrial enterprises, or to lend only at very high costs, for two main reasons. Firstly, without a credit history banks face difficulties in assessing the credit risks of borrowers. Secondly, agricultural companies have little available collateral to mitigate the risks of financing.

The gap for debt finance in the Portuguese economy was assessed to be between EUR 3 billion and EUR 5.5 billion, with significant share of it in the primary sector (see Chapter 3.1). Setting up an FoF was designed to tackle part of this financing gap. The managing authority appointed the European Investment Fund (EIF) as manager of the FoF and requested them to launch a portfolio guarantee instrument as a pilot initiative. The portfolio guarantee is implemented via four selected financial institutions under conditions stipulated in operational agreements they signed with the EIF.

The financial instrument provides capital relief via loss protection for financial institutions with a capped guarantee of 70% on a loan-by-loan basis up to a maximum amount, based on a maximum cap rate. The cap rate is agreed with each financial institution individually. In exchange for the guarantee, the financial institutions commit to build a portfolio of new loans or finance leases (hereinafter collectively referred to as loans). The financial instrument aims to finance investments in agricultural holdings, as well as for processing, marketing and/or development of agricultural products. The benefit of the guarantee is transferred to final recipients in the form of reduced interest rates, lower collateral requirements, longer maturities and/or longer grace periods.

The financial instrument is expected to increase the leverage of EU funds for agriculture and agri-businesses with a target loan portfolio of EUR 315 million. The first disbursement to final recipients was in June 2020. Shortly after the launch of the instrument, flexibility measures were introduced in relation to the COVID-19 pandemic. These followed changes in EU legislation (such as the possibility to provide stand-alone working capital) in particular to support small and medium-sized enterprises (SMEs) impacted by the crisis. As of 30 June 2021, 100 loans to final recipients have been committed for a total of EUR 35 million (half of which has been disbursed). The guarantee cap for these is EUR 3.5 million.

Portuguese EAFRD Guarantee Instrument

THE FINANCIAL INSTRUMENT

Funding sources

EAFRD RDP 2014-2020 Portugal
EFSI

Type of financial products

Capped portfolio guarantee for loans and finance leases

Financial size

EUR 20.07 million contribution from the RDP (of which EUR 18.53 million is from EAFRD and EUR 1.54 million from the national budget) and up to EUR 15 million from EFSI.
The financial instrument is expected to support a loan portfolio of up to EUR 315 million.

Thematic focus

Investments in primary agricultural production or for processing, marketing and/or development of agricultural products.

Timing

From 2019 to 2023

Partners involved

Portuguese Republic Ministry of Agriculture (managing authority)
EIF (FoF manager)
Banco BPI, Caixa Geral de Depósitos, Caixa Central de Credito Agricola Mutuo and Banco Santander Totta (financial institutions)

ACHIEVEMENTS

EU leverage[1]

17 times

Leverage of public resources[2]

9 times

Main achievements

As of 30 June 2021, 100 loans had been committed to final recipients for a total of EUR 35 million, for which the guarantee cap was EUR 3.5 million. The total cumulative disbursements were EUR 18 million. Of the committed loan agreements so far, 79% of the final recipients are microenterprises, 13% are small enterprises, 6% are medium-sized enterprises, while 2% are Mid-caps. The average loan amount committed so far is approximately EUR 350 000. As of September 2021, there was an estimated pipeline of 400 additional operations.[3]

1 EU leverage is calculated as the total amount of finance to eligible final recipients, i.e. EUR 315 million (based on the maximum portfolio size), divided by the total EAFRD allocation to this financial instrument, i.e. EUR 18.53 million, gross of management fees. It does not include the reuse of resources returned to the instrument.

2 Leverage of public resources is calculated as the total amount of finance to final recipients, i.e. EUR 315 million (based on the maximum portfolio size), divided by the total public resources allocated to the financial instrument, i.e. EUR 35.07 million, gross of management fees. It does not include the reuse of resources returned to the instrument.

3 Based on the number of requests for declaration of conformity for RDP operations submitted to the managing authority, which is a prerequisite for a loan under the financial instrument.

2. Objectives

In Portugal, the ex-ante assessment[4] highlighted a shortage of credit for all sectors with a financial gap estimated at EUR 3 billion to EUR 5.5 billion for the whole economy. The fi-compass study in 2020[5] focusing exclusively on the agricultural and agri-food sectors, confirmed a significant financing gap of EUR 829 million to EUR EUR 1 117 million in these sectors.

The drivers of this financing gap include (i) high investment risks due to volatile market prices and activities not covered by insurance, (ii) insufficient collateral (especially for smaller farms and new entrants with limited assets), (iii) a lack of credit history and/or accounting records, and (iv) a lack of financial knowledge and business management skills. This is worsened by the high indebtedness of Portuguese companies in all sectors (according to the ex-ante assessment, about 30% of microenterprises, 25% of SMEs and 20% of larger companies have overdue loans). These issues underline the importance of guarantee instruments and their particular relevance for the agricultural sector.

The ex-ante assessment envisaged three main objectives for financial instruments in the framework of the RDP, to: i) promote entrepreneurship, especially for young farmers, ii) increase agricultural added value through the development and implementation of new farming business models and iii) reinforce the positions of companies in value chains. There is further information on the ex-ante assessment in Chapter 3.1.

The key objective for the managing authority was to design an effective financial instrument with competitive features and attractive conditions to ensure the adequate involvement of financial institutions as well as efficient uptake by final recipients. Due to the limited resources available under the RDP, leverage was also very important with the possibility of mobilising additional resources.

To benefit from additional resources, the managing authority decided to join the EAFRD-EFSI Initiative, a platform launched in 2016 by the Directorate-General for Agriculture and Rural Development of the European Commission in cooperation with the EIB Group. The goal of the Initiative was to deepen the strategic focus on financial instruments in the agricultural and agri-food sectors and to stimulate greater allocations of EAFRD resources to financial instruments. This initiative offered a comprehensive package for managing authorities, including a free of charge feasibility study prepared by EIB (under fi-compass), the potential to mobilise EFSI resources and reliance on EIF expertise for product deployment[6].

4 Ex-ante assessment of the Financial Instruments of the Portugal 2020 Programmes: Lot 1 - Financial Instruments for direct support to companies.

5 fi-compass, 2020, 'Financial needs in the agriculture and agri-food sectors in Portugal'.

6 More information available at: https://www.fi-compass.eu/news/2016/12/new-eu-investment-initiative-boost-financing-rural-economy.

3. Design and set-up

To address the financing gap for farmers and agribusinesses the RDP managing authority entrusted the EIF with the creation of an FoF to implement one or more financial instruments. In parallel, the managing authority submitted RDP amendments to the European Commission (EC) to ensure consistency with the financial instrument.

Having received formal approval of the RDP amendments from the EC, a funding agreement was signed between the managing authority and the EIF on 3 May 2019. This included the investment strategy and business plan for implementation of a portfolio guarantee instrument within the FoF structure.

The EIF launched the call for expression of interest to select financial institutions active in the target market on 16 July 2019. Eligible and interested financial institutions could submit their applications up to 27 August 2019.

Following the selection process, three operational agreements were signed in March 2020, followed by a fourth in July 2020.

Disbursement to final recipients started in Q2 2020, with the first loan agreement signed in June 2020.

Following the emergence of the COVID-19 health crisis, the European Commission proposed changes to the Common Provisions Regulation (CPR) and EAFRD Regulations which were accepted by the co-legislators. These allowed the provision of stand-alone working capital finance under EAFRD financial instruments for SMEs negatively affected by the crisis. As a consequence, the managing authority introduced amendments to the RDP in October 2020 enabling the financial instrument to support immediate liquidity needs of agricultural SMEs.

Table 1: Timeline for setting up the financial instrument

Date	Event
April 2015	Ex-ante assessment for the use of financial instruments in RDP 2014-2020
May 2019	Funding agreement signed between the EIF and the managing authority
July 2019	Publication of the call for expressions of interest to select financial intermediaries
August 2019	The call for expressions of interest closed
March-July 2020	Operational (guarantee) agreements signed between the EIF and selected financial institutions
June 2020	First disbursement to final recipients
October 2020	Amendments in response to the COVID-19 crisis

3.1 Ex-ante assessment

The ex-ante assessment covered the potential implementation of financial instruments for Portugal 2014-2020 Programmes under ESIF. These included the Competitiveness and Internationalisation Operational Programme (OP) and Regional OPs together with the RDPs for Mainland Portugal, Azores and Madeira.

The objective of the study was to verify the existence of market failures and sub-optimal investment situations related to the availability of financing, financing costs, and capitalisation levels of Portuguese enterprises, including agricultural and agri-industrial companies.

In 2018, the primary sector in Portugal accounted for 2.3% of total Gross Value Added and 4% of employment in the country. The main product types are fruits and vegetables, wine, dairy and animal production including cattle, pigs and poultry. Farms in Portugal are predominantly small-sized and family owned, with 90% below 20 hectare. Smaller farms are concentrated in the Northern regions of the country, whereas large companies are more often found in the South.

The contribution of the agri-food sector to the Portuguese economy is significant, especially within the manufacturing industry. The main activities are animal slaughter, meat preparation and preservation, followed by baking and the dairy industry. The majority (97%) of the companies are small, employing less than 50 people.

According to the ex-ante assessment, Portuguese enterprises generally have insufficient capital and high indebtedness, which makes it difficult to access financing and brings higher financing costs. During the early 2010s, in the aftermath of the global financial crisis, economic activities diminished in Portugal, accompanied by a general freeze for financing and investment. As a result, companies in Portugal, and SMEs in particular, have faced the double challenge of recovering from the recession and returning to economic growth while reducing bank debt.

The recommendation of the ex-ante assessment was to implement a wide range of financial instruments to respond to the different needs of companies looking to finance investment projects. Enterprises in the agricultural and agri-industrial sector faced a shortage of available financing and high financing costs compared to the average profitability of the sector. This led to a recommendation in the ex-ante assessment for the use of guarantee instruments.

Any financial instrument set up under the EAFRD was expected to reduce the shortage of financing from the financial market, diminish the higher risks banks associated with agricultural activities and therefore improve financing conditions for companies in these sectors.

3.2 Selection of the implementing body

The EIF was appointed directly by the managing authority as FoF manager pursuant to Article 39a(5)(b) and Article 38(4)(b)(i) of the CPR[7]. The legal basis for setting up the instrument was Article 38(i)(c) of the CPR (as amended by Regulation No. 2018/1046[8]) taking into account the combination of the financial contribution provided by the managing authority through its RDP together with EFSI resources.

7 The Managing Authority may entrust implementation tasks, through the direct award of a contract to the EIB Group.

8 Regulation (EU, Euratom) No. 2018/1046 of the European Parliament and of the Council of 18 July 2018 on the financial rules applicable to the general budget of the Union, amending Regulations (EU) No. 1296/2013, (EU) No. 1301/2013, (EU) No. 1303/2013, (EU) No. 1304/2013, (EU) No. 1309/2013, (EU) No. 1316/2013, (EU) No. 223/2014, (EU) No. 283/2014, and Decision No. 541/2014/EU and repealing Regulation (EU, Euratom) No. 966/2012 referred as 'Omnibus Regulation'.

The investment strategy and business plan in the funding agreement called for a First Loss Portfolio Guarantee, under a delegated model (see Chapter 4.3) via selected financial institutions.

To fine-tune the financial instrument and maximise its suitability for the market, the EIF carried out comprehensive market testing following the signature of the funding agreement. This review the possibility of both a capped and an uncapped guarantee instrument from the perspective of market player interest, absorption capacity and expected risk profiles.

In parallel, RDP amendments were submitted to the EC for approval, defining the sub-measures of the RDP from which the financial instrument would be funded, the objectives, target beneficiaries and eligibility criteria.

Following the market testing, the EIF launched a call for expression of interest to identify, evaluate and select financial institutions to implement the FoF financial instruments. The selection was conducted in three phases. First was a pre-selection phase where the expressions of interest were evaluated according to formal eligibility criteria (e.g. place of operation, financial standing) as well as the quality of the application (e.g. implementation strategy, credit processes). This was followed by a due diligence process of applicants which assessed – among others – their track record in the agricultural sector, their ability to build up the envisaged portfolios, as well as their proposed approach to transfer benefits to final recipients. In the third and last phase the EIF either selected, placed on the reserve list or rejected each expression of interest.

Following this process, four financial institutions were selected, namely Banco BPI, Caixa Geral de Depósitos, Caixa Central de Credito Agricola Mutuo and Banco Santander Totta, and the operational agreements were signed in March - July 2020.

3.3 Funding and governance

The instrument combines an RDP contribution of EUR 20.07 million with EFSI funding of up to EUR 15 million. The latter funding is available thanks to the EAFRD-EFSI Initiative via the EFSI SME Window. Actual use of the EFSI funding is subject to reaching a certain portfolio volume, which would justify the need for added coverage by the guarantee.

Table 2: Funding sources and amounts

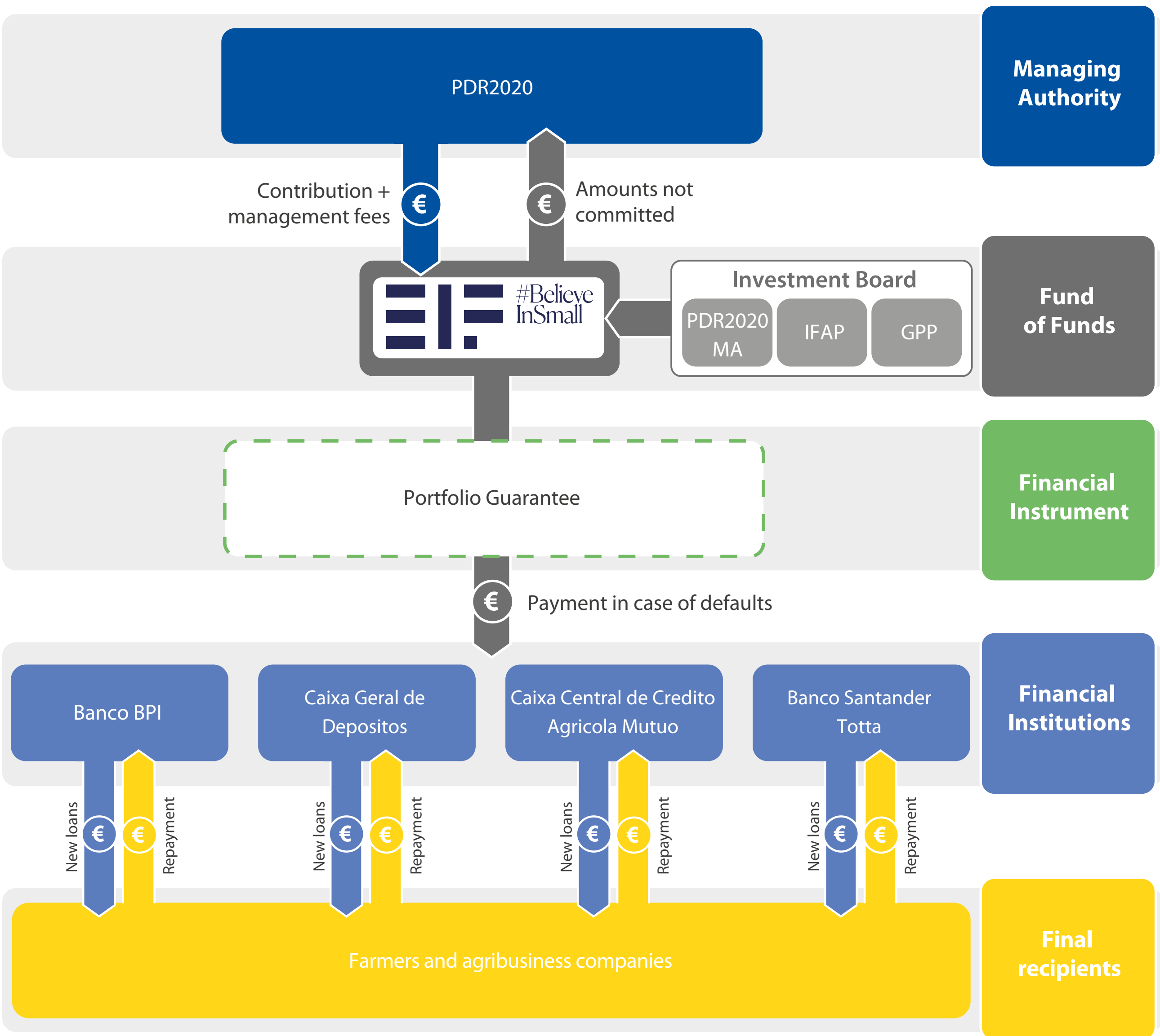
Funding source	Amount
RDP Contribution	EUR 20 066 861
of which, EAFRD	EUR 18 525 726
of which, national co-financing	EUR 1 541 135
EFSI	Up to EUR 15 000 000
Financial institutions	Up to EUR 280 000 000

Source: Funding Agreement, Operational Agreements.

The managing authority and the EIF signed a funding agreement authorising the EIF to manage the amounts made available to the FoF in its own name but on behalf of the Member State. The funding agreement also defines the investment strategy and business plan, the rules of governance, the exit strategy and rules in relation to monitoring and audits.

The governance of the instrument is through an investment board of three members, appointed and empowered by the Member State. The members are representatives from the managing authority, the Paying Agency – Instituto de Financiamento da Agricultura e Pescas, I.P. (IFAP) and Cabinete de Planeamento, Políticas e Administração Geral (GPP). The investment board approved the terms of the call for expression of interest and continuously monitors and supervises implementation of the investment strategy and business plan.

Figure 1: Governance structure of the Portuguese 2014-2020 EAFRD financial instrument



Source: Funding Agreement, Operational Agreements.

4. Implementation

The EIF in its role as FoF manager provides the selected financial institutions with a capped guarantee to cover part of the losses on portfolios of newly originated loans to eligible final recipients in the agricultural and agri-industrial sectors.

In return for the guarantee, the financial institutions are required to improve the conditions of bank credit for the final recipients. The improvement is through interest rate reductions thanks to a lower cost of capital and credit risk for the banks on the guaranteed portion of each loan. The banks must also lower the required collateral compared to their standard credit policy. In addition, the operational agreements request the financial institutions offer longer maturities and longer grace periods.

Importantly, each financial institution should achieve a target portfolio volume. The EIF determines a maximum portfolio volume as well as an agreed portfolio volume for each financial institution, which is defined in their operational (guarantee) agreement. The portfolio volume for each financial institution is the size of the portfolio of loans for which the guarantee is currently committed. This can be adjusted in line with disbursements, prioritising financial institutions with better performance, up to their maximum portfolio volume. Starting from signature of the operational agreement, the financial institutions have 36 months to build up the loan portfolio.

Initially the investment strategy did not allow a combination of support under the financial instrument with other forms of support such as RDP grants. However, due to the economic crisis caused by the COVID-19 pandemic, from October 2020 this provision was changed and such combinations were allowed respecting the cumulation rules. In addition, to support the liquidity needs of target businesses, in line with the Coronavirus Response Investment Initiative (CRII) amendments[9], stand-alone working capital can be financed up to EUR 200 000 for SMEs impacted by the crisis until 30 June 2022.

4.1 Financial products and terms

The financial product is a capped portfolio guarantee with a 70% guarantee rate that is free of charge thanks to the contribution of funding from the RDP of Mainland Portugal. The guarantee covers each eligible loan in the portfolio on a transaction-by-transaction basis. The maximum liability of the FoF is limited to a percentage (Cap Rate) of the guaranteed share of the portfolio agreed with each financial institution (between 13% and 17% for this guarantee instrument). Since the guarantee is linked to a share of the portfolio built up by the bank, the guarantee cap amount is proportional to the actual portfolio size. So, the larger the portfolio, the larger the guarantee cap amount.

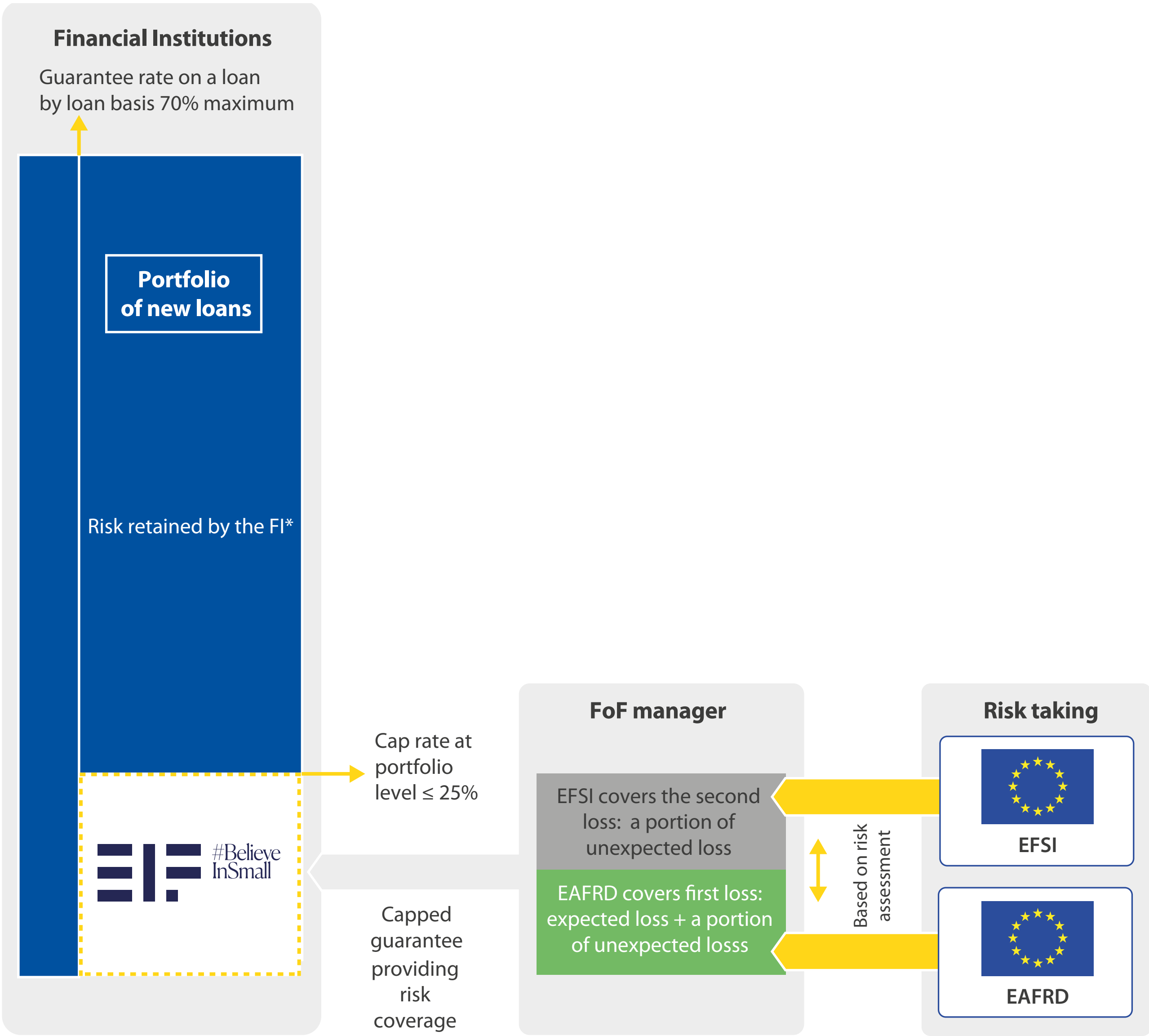
The EFSI component in the structure is complementary to the EAFRD funding (in line with the principle of additionality). This means its risk coverage is senior to the first loss piece taken by the RDP allocation and can be used only after the RDP contribution is fully absorbed. This way, the new loans offered to final recipients can be increased by an additional EUR 145 million, potentially totalling EUR 315 million, increasing the market impact by 85%. Due to the relatively low cap rates agreed with the financial institutions, the expected leverage on the RDP resources is 16 times (and 17 times considering only EAFRD funding).

9 In relation to the COVID-19 outbreak, to rapidly mobilise ESI Funds to combat the health and economic crisis, European co-legislators approved amendments to the CPR as part of the CRII and CRII Plus package. The first amendments set out in Regulation (EU) No. 2020/460 came into force on 31 March 2020, while the second amendments implemented by Regulation (EU) No. 2020/558 have been in force as of 24 April 2020.

The conditions for the guarantee stipulate that the new loans support investments and costs eligible under the relevant sub-measures of the RDP and that the benefit of the guarantee is transferred to final recipients. The banks must offer better financing conditions compared to their standard loans (such as longer maturities, longer grace periods, reduced interest rates, lower collateral or a combination of these) for farmers and food processors.

The banks may only include transactions in the portfolio approved during the availability period, which is 36 months from signature of their operational agreement. The guarantee coverage is provided for the principal amount disbursed by 31 December 2023.

Figure 2: The product mechanism



Source: Annex III to the Open Call for Expression of Interest to Select Financial Institutions, 2019.

Note: *Financial Institution (FI).

Loan provided under the guarantee can be from EUR 25 000 to EUR 5 million for operations under sub-measure M4.1 'Support for investments in agricultural holdings' and up to EUR 10 million for operations under sub-measure M4.2 'Support for investments in processing, marketing and/or development of agricultural products. The loan maturity (i.e. the maximum time for repayment) can be between 3 and 15 years, but not beyond 31 December 2035.

Table 3: Financial product key characteristics

Loan amount	Minimum: EUR 25 000 Maximum: EUR 5 million for Operations 3.1.3 and 3.2.3 (see below) Maximum: EUR 10 million for Operation 3.3.3
Guarantee rate	70% (of the loan amount on a transaction-by transaction basis covering final losses up to the cap)
Cap rate	13-17% as agreed with each financial institution.
Maturity	Between 3 and 15 years (but not beyond 31 December 2035)
Eligible final recipients	Farmers and businesses carrying out investments for the transformation, marketing and development of agricultural products
Eligible operations	Operation 3.1.3 'Investment of Young Farmers in agricultural holdings supported by a financial instrument' included in the sub-measure M4.1 Operation 3.2.3 'Investment in agricultural business supported by a financial instrument' included in the sub-measure M4.1 Operation 3.3.3 'Investment in transformation and marketing of agriculture products[10] supported by a financial instrument' included in sub-measure M4.2
Availability Period	36 months (to build up the loan portfolio, starting from signature of the operational agreement)

The loans under the instrument are available for economically viable natural persons (e.g. individual farmers, including young farmers) or legal persons carrying out economic activities in Mainland Portugal.

Each loan can support investments under three operations: 3.1.3 Investment of young farmers in agricultural holdings supported by a financial instrument included in sub-measure M4.1, or 3.2.3 Investment in agricultural business supported by a financial instrument included in sub-measure M4.1, or 3.3.3 Investment in transformation and marketing of agriculture products supported by a financial instrument included in sub-measure M4.2.

The financial instrument provides support to young farmers (aged between 18 and 40) that are head of a farm holding, have appropriate vocational training and have not been in the farming business from more than five years. For long-established farm businesses (outside young farmers), the eligibility requirements include a registered farming activity that is also registered in the parcel identification system. To be eligible for support, food processors should have a relevant economic activity to carry out investments in the transformation and marketing of agricultural products.

10 Agricultural Products means products listed in Annex I to the TFEU, with the exception of fishery and aquaculture products covered by Regulation (EU) No. 1379/2013.

Loans provided under the instrument can support investments in tangible and intangible assets[11] including general costs[12], as well as working capital ancillary to the investment project[13]. In addition, loans to SMEs impacted by the COVID-19 pandemic from October 2020 are eligible for stand-alone working capital support up to EUR 200 000 per final recipient.

The instrument can also support the acquisition of second-hand and replacement equipment. The purchase of land is also eligible up to 10% of the total eligible expenditure of the investment for transactions falling under sub-measure M4.1, with the additional limitation that for investments in established agricultural businesses only parcels being re-arranged are eligible for land acquisition.

Ineligible costs include fines, financial penalties, legal and litigation costs, charges, premiums, tariffs and costs related to a leasing contract. However, VAT paid by the final recipients is eligible under the financial instrument (unlike for grants under the RDP).

Since October 2020 it has been possible to combine the financial instrument with RDP grants, when final recipients have received approval for grant support from the 2014-2020 RDP[14].

4.2 State aid

In line with EU regulations, support (including stand-alone working capital finance) provided under the financial instrument is exempted from State aid rules. This is because the financial instrument can only support activities related to agricultural products (included in Annex I of the TFEU), where State aid rules do not apply. However, aid intensity thresholds should be respected, which means that the Gross Grant Equivalent (GGE) of each loan in the portfolio should not be higher than a pre-defined proportion of the eligible costs of the investment. If the final recipient has more than one transaction supporting the same investment, these are cumulated.

The aid intensity threshold depends on whether the loan is stand-alone or combined with grant support.

For stand-alone loans, which are not combined with grants from the RDP, the maximum aid is 35% of the eligible costs of the investment. For combinations of financial instrument and RDP grant support, the sum of the grant support and the GGE of the guaranteed loan shall not exceed the aid intensity threshold. The thresholds are set out in the RDP in line with Annex II of Regulation (EU) No. 1305/2013 and defined by the managing authority in a declaration of conformity based on the characteristics of the final recipient.

11 In line with the RDP, the instrument does not support the processing of non-agricultural products as input nor output, projects concerning fishery or aquaculture products, investments mainly for energy production, investments in annual plants, or in live animals with the exception of autochthonous breeds in the context of operation 3.1.3. Pure financial transactions, including consumer credit and real estate development as a financial investment activity are also excluded from the scheme.

12 General costs include architect, engineer and consultation fees as well as fees relating to advice on environmental and economic sustainability, including feasibility studies.

13 The total expenditure for working capital cannot exceed EUR 200 000, or 30% of the total eligible costs for the investment, whichever is the higher.

14 The RDP operations for the combination are:
- 3.1.2. 'Investment of Young Farmers in agricultural holdings';
- 3.2.1. 'Investment in agricultural businesses';
- 3.2.2. 'Small investments in agricultural businesses';
- 3.3.1. 'Investments in the transformation and marketing of agriculture products';
- 3.3.2. 'Small investments in the transformation and marketing of agriculture products'.

4.3 Financial flow and appraisal process

According to the CPR[15], the Member State can request the first interim payment of up to 25% from the EC after signature of the funding agreement. Submission of subsequent interim payments are conditional on proof that 60% of the initial contribution, then 85% of all subsequent payments have been used by the financial instrument. To ensure uninterrupted funding flows for the purpose of building up the final recipient portfolios, the funding agreement defined a payment schedule differing slightly from the payment flow between the Member State and the EC. This complies with the legal requirement for contributions to be split in tranches and linked to disbursements to final recipients. The rationale for this payment schedule was for the financial institutions to continue originating new loans if absorption by one or more of them is faster than payments from subsequent tranches.

Accordingly, the phased payment schedule to the FoF is as follows:

- The first tranche of 25% of the RDP contribution committed in the funding agreement, was paid upon its signature by the managing authority and the EIF.
- The second tranche, for the next 25% of the RDP contribution, was made available on the approval of the first operational agreement.
- The third tranche, for the next 25%, is paid once at least 60% of the first tranches has been used.[16]
- The fourth tranche, for the last 25%, is paid once at least 85% of the first two tranches has been used.

The guarantee provided under the financial instrument is unconditional and irrevocable. In case of default, the financial institutions receive a payment equal to the default amount of each covered loan, multiplied by the guarantee rate, until the guarantee cap on the portfolio is reached.

The financial instrument is implemented under the delegated model, which means the financial institutions appraise loan applications prior to commitments to final recipients. Individual loans have to comply with eligibility criteria defined in the operational agreements in line with the funding agreement (e.g. related to the final recipients, investment project, expenditure and the relevant sub-measure of the RDP). To include loans in the guaranteed portfolio, the financial institutions check compliance with these criteria.

Certain supervisory tasks are nevertheless carried out by the EIF as FoF manager, including monitoring visits. A control report[17] is also provided by the EIF to support interim payment claims by the Member State to the EC according to Article 41 of the CPR. The control report includes a list of loans to final recipients as reported by the banks, amounts committed as well as the state of implementation, a progress analysis and a summary of the monitoring activities and resulting follow-up actions.

15 Article 41(1) of Regulation (EU) No. 1303/2013.
16 Funds 'used' means they have been allocated to cover possible losses of financial institutions corresponding to amounts disbursed to final recipients or have been used to pay management fees.
17 As defined by the Implementing Regulation (EU) No. 2019/1140 referred to in Article 40(1) of the CPR.

4.4 Operational guidance

To streamline implementation of the financial instrument and to provide technical support for the participating banks, the managing authority developed an operational guidance note for compliance with EU and national laws and regulations, including the relevant RDP provisions.

The guidance note contains definitions and technical interpretations, including for documentary evidence in relation to specific eligibility requirements. Financial institutions and final recipients are guided to the relevant documentary evidence based on the investment project specificities.

The eligibility criteria include the requirement for the final recipient to provide a declaration of conformity issued by managing authority/paying agency to the banks prior to signing the loan contract. The declaration is based on information in the IACS[18] IT system of the paying agency and the guidance note includes templates of declarations for each of the three operations under the financial instrument.

According to the terms of the guarantee, the banks must include evidence of compliance with applicable laws and regulations in the documentation for each loan contract. The evidence can be undertakings, representations and warranties from final recipients. Final recipients should also present documents to the banks confirming any specific authorisation if required for the investment. The guidance package includes a comprehensive list of these documents, certificates and authorisations. The managing authority has also developed templates for self-declarations by the final recipient to be submitted to the banks to confirm the nature of the proposed investment (e.g. whether or not it involves construction) and the authorisations required under the applicable laws and regulations.

The operational guidance helps participating banks to request the necessary documentation, authorisation, certificates, etc., depending on the investment project. It also provides additional assurance, as certain eligibility criteria can be confirmed in the declaration by the authorities prior to submitting applications to the financial institutions.

18 Integrated Administration and Control System.

5. Output

The disbursement of loans under the instrument started in June 2020. Based on the quarterly inclusion reports provided by the banks to the EIF, as of 30 June 2021, 100 final recipients had received loans for a total of EUR 34 682 953. The average loan is for approximately EUR 350 000 (see Table on page 5).

In terms of distribution by economic activity, 45% of final recipients grow perennial crops (mainly olives and nuts), 10% are in wine production, 11% in mixed farming and 8% in animal production. The rest grow non-perennial crops and vegetables, process meat, oils and dairy or wholesale food and beverages. Overall, 83% of final recipients, of which almost one in five are young farmers, received loans for investments under sub-measure M4.1. The remaining 17% of final recipients received support for investments in the transformation and marketing of agricultural products under sub-measure M4.2.

Based on the number of employees and annual turnover, 79% of the final recipients are micro enterprises, 13% are small enterprises, 6% are medium-sized enterprises, while 2% are considered Mid-caps. There is a balanced territorial distribution of the funds, with 45% of the investments in the South and 55% in the Central and Northern part of the country.[19]

MOB - Moreira, Olazabal & Borges, Lda.

Type of finance: Investment loan with working capital component

Purpose of the loan: Purchase of new equipment and technology for the winery

Total value of the investment: EUR 400 000

Loan amount: EUR 280 000

Maturity: 8 years

Grace period: 24 months

The final recipient is a joint venture of three wine producers: Jorge Moreira (Poeira), Francisco Olazabal (Quinta do Vale Meão) and Jorge Serôdio Borges (Wine & Soul).

The investment is financed by a loan from Banco BPI and increases and improves fermentation capacity with new vats that have a temperature control system.

Additional French oak barrels to store and age the wines will generate added value in wine production.

The investment will also improve conditions in the warehouse, with modernisation of the electrical system and thermal insulation. The working capital component finances the acquisition of raw materials to increase production.

Source: Banco BPI, 2021.

19 This data will be updated with the progress in implementation of the financial instrument.

Investment to expand avocado orchards

Type of finance: Investment loan

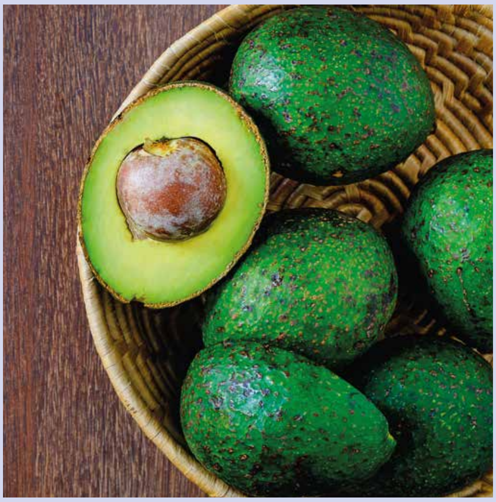
Purpose of the loan: Expansion of orchards for avocado production

Total value of the investment: EUR 706 248

Loan amount: EUR 600 000

Maturity: 10 years

Grace period: None



The final recipient is an agricultural producer in Algarve with three generations of orchard farmers in the family business.

The investment, enabled by a loan from Caixa Geral de Depósitos, covers initial expenses to expand the orchards by planting 57 hectares of avocado in a hyper intensive system. The orchards have direct access to water from the Bravura dam in Algarve, which guarantees sufficient resources to supply the farm. The production process complies with health, environment and biosafety standards, so it is eligible for agro-environmental subsidies as well.

The avocados are stored in ethylene cold rooms to preserve them in better condition. This gives greater bargaining power with large supermarkets due to greater flexibility in timing sales. With these investments, the final recipient intends to increase profitability and reduce costs through economies of scale.

Source: Caixa Geral de Depósitos, 2021.

6. Lessons learned

The EAFRD guarantee instrument presented here is a good example of a public support scheme encompassing a result-oriented, market-driven financial product with compliance-based implementation following eligibility rules defined according to specific policy goals. The product features were designed in line with market needs (substantiated by a thorough market assessment) to respond to market failures and suboptimal investment situations identified in an ex-ante assessment and study. Based on a dedicated investment strategy focusing on the agricultural sector, a tailor-made instrument was developed to improve competitiveness and increase added value for agricultural producers as well as agri-food processors and to ensure generational renewal in farming. In this respect, support for the acquisition of machinery and equipment, agri-technology uptake, land purchase and enhanced soil and water management systems are particularly important, especially for young farmers.

Prior to the launch of the guarantee instrument, studies had shown that the strong tradition of non-repayable support in the agriculture sector meant target beneficiaries had little knowledge of financial instruments. Thanks to a well-designed product with attractive financing conditions as well as effective communication campaigns by the participating financial institutions, the appetite for such support to complement, or even substitute grants, has increased. This is highlighted by the number of applications in the pipeline which shows a growing interest from final recipients.

The complementary nature of the guarantee product is also seen in terms of timing. The financial instrument provided targeted support for farmers and agri-industrial companies when alternative EU sources were not available due to a shortage of budget allocation within the RDP grant schemes, or a lack of open grant application windows. In such cases, the guarantee instrument proved to be a flexible source of funding for businesses and investment projects.

The flexibility of the instrument was demonstrated by the measures introduced following the COVID-19 outbreak. Seizing the opportunity offered by updated EU regulatory provisions, the financial instrument investment board adapted the eligibility rules. These now allow financing for stand-alone working capital that addresses immediate liquidity needs of companies as well as support for investments that have already received RDP grants.

The operational guidance and streamlined procedure are good examples of enhanced cooperation among the different actors involved in the implementation process, and a helpful tool for financial institutions aligning their standard banking practices to formal regulatory requirements.

The guarantee instrument shows that an efficient use of public funds and exploiting leverage mechanisms, means relatively limited resources can create significant market impact. The introduction of the EAFRD-EFSI Initiative by the EC, and the possibility to combine EAFRD funds with resources from EFSI enables a larger loan portfolio, attracting additional resources from financial institutions and increasing the impact on the ground.

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