



**Expert evaluation network  
delivering policy analysis on the  
performance of Cohesion policy 2007-2013  
Year 2 – 2012**

**Task 1: Financial engineering**

**Romania**

**Version: Final**

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**A report to the European Commission  
Directorate-General Regional Policy**

## Contents

Executive summary .....	3
1. Use of financial engineering instruments .....	4
2. Rationale for using financial engineering instruments .....	5
3. The effectiveness of financial engineering instruments: selected examples .....	7
4. Main problems in using financial engineering instruments .....	12
5. Evaluations of financial engineering instruments .....	12
6. Concluding remarks.....	13
References .....	14
Interviews.....	15
Annex.....	15

## List of abbreviations

- ACIS Authority for Coordination of Structural Instruments
- EEN Expert Evaluation Network
- EIF European Investment Fund
- FA Funding Agreement
- FEI Financial Engineering Instrument
- FLPG First Loss Portfolio Guarantee
- HF Holding Fund
- KAI Key Area of intervention
- MA Managing Authority OP Operational Programme
- MECBE Ministry of Economy Commerce and Business Environment
- MS Member State
- MoPF Ministry of Public Finance
- NGF National Loan Guarantee Fund for SMEs
- R&D Research & Development
- RLGf Romanian Loan Guarantee Fund
- ROP Regional Operational Programme
- SI Structural Instruments
- SOP IEC Sectorial Operational Programme Increase Economic Competitiveness
- OP Operational Programme
- VC Venture Capital

## Executive summary

Financial engineering instruments (FEIs) funded by the Cohesion policy 2007–2013, in Romania, are implemented through the Sectorial Operational Programme Increase of Economic Competitiveness (SOP IEC), Key Area of Intervention (KAI) 1.2 SMEs access to finance.

There are two types of FEIs implemented in Romania. Both of them are FEIs for enterprises: loan guarantee instruments and venture capital funds. They are implemented through a holding fund, within the EU JEREMIE initiative. The management of the JEREMIE fund was awarded, by the Romanian Government to the European Investment Fund (EIF). The choice of the EIF was based on its know-how in FEIs implementation, its credibility on the capital markets, the low management costs, etc.

The FEIs rationale is built on the severe undercapitalisation of the SMEs in Romania. There are four market gaps: debt/financing guarantees, micro lending, venture capital, and technology transfer.

Despite the late and difficult start, at the end of 2011, JEREMIE Romania set up four instruments: three guarantee agreements with three banks and one risk capital fund. The entire budget was contracted with the financial intermediaries. The additional resources committed by the guarantee instruments at the level of the final recipients, from outside the operational programme, amounted to EUR 322 million. 142 SMEs were registered, as support recipients, through the loan guarantee instrument.

Being a new instrument in Romania, JEREMIE encountered a number of difficulties. There were difficulties with the regulatory issues, the application of the EU eligibility rules, the negotiations with the private investors, etc. Lessons learnt from the JEREMIE implementation may be very important for extending FEIs in the Cohesion policy programmes.

FEIs have a great potential to complement the current instruments, and enhance the support to enterprises, and regions. The key benefits of FEIs in an operational programme are the recycling of funds and the availability of the support over a longer duration. . The grant schemes continue to be essential for the strategic sectors, and the market segments with a low investment return or a high level of risk.

Before extending the use of FEIs in the future Cohesion policy, the stakeholders willingness and capacity to contribute to the process of change must be taken into account. As FEIs are not as well-known as grants, some stakeholders may be reluctant to replace grants with FEIs, unless the benefits for each stakeholder are clearly presented.

## 1. Use of financial engineering instruments

FEIs, supported by Cohesion policy 2007 – 2013 in Romania, are implemented through the SOP IEC, KAI 1.2 SMEs access to finance. The total allocation for 2007-2013 amounts to EUR 100 million, representing 1% of the total ERDF allocation for Romania, 3.9% of ERDF allocation for SOP IEC, and 10.8% of the total ERDF allocation for Priority Axis 1 - An innovative and eco-efficient productive system. The support is provided within the JEREMIE initiative launched by DG Regio and the EIB Group.

### *FEIs with a holding fund*

FEIs are implemented through a holding fund, referred to as JEREMIE Holding Fund. The Romanian Government awarded the management of JEREMIE Holding Fund to the European Investment Fund<sup>1</sup>, the Funding Agreement was signed on 18 April 2008.

The SOP IEC (KAI 1.2) highlights the need for an appropriate mix of instruments, as identified in the gap assessment leaving to JEREMIE strategic management the responsibility for identifying the most appropriate ones, and creating the portfolio of instruments. The initial proposal, part of the Funding Agreement between the Romanian Government and EIF, included two instruments:

1. *A guarantee instrument, First Loss Portfolio Guarantee (FLPG) Instrument*, including *guarantee agreements*, with an approximate allocation of EUR 65 million; The instrument is implemented under a state aid “de minimis” scheme, approved by the Ministry of Economy Commerce and Business Environment (MECBE) in July 2010.
2. *A hybrid Venture Capital Instrument, referred to as Risk Capital Instrument* in the JEREMIE Romania programme documents, including venture capital funds with an initial allocation of EUR 35 million; at the reporting date, one financial intermediary had been contracted and one risk capital fund had been set up, expected to become operational in the second quarter of 2012.

### *Changes during implementation*

Due to the difficulties encountered in setting up one of the risk capital funds, and a higher absorption potential of the guarantee instruments, in 2011 EIF reallocated within the JEREMIE Fund, EUR 17.5 million from Risk Capital instrument to FLPG Instrument.

According to the MA for SOP IEC, a reallocation of an additional EUR 50 million to the JEREMIE Fund, on top of the EUR 100 million, is being considered at the present, in the context of identifying the most effective measures for increasing absorption.

### *Other FEIs supported by Cohesion policy*

The opportunity and feasibility for a new *FEI for urban development* were analysed during the last 2 years, by the Growth Pole Brasov in Region Centre. The analysis considered the support of Cohesion policy through the Regional Operational Programme within the JESSICA initiative. In 2010, the European Investment Bank (EIB) commissioned Deloitte Romania to produce an evaluation study on JESSICA practical implementation issues. For the current cycle 2007 – 2013, the initiative was abandoned, further analysis being necessary for the 2014+ options in implementing urban development FEIs.

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<sup>1</sup> Government Decision 514/2008

Romania, as a new Member State (MS) is implementing Structural Instruments during the 2007–2013 programming cycle for the first time. The pre-accession programmes supported few financial engineering operations on a much smaller scale, isolated initiatives (loan schemes with a non-reimbursable component and subsidised interest rates):

1. The Loan Pilot scheme for SMEs, Phare RO9711 and RO2000, launched in 2003, EUR 11.4 million, closed in 2009<sup>2</sup>
2. The MARR Fund (Mining Affected Regions Reconstruction Fund), Phare 1998, EUR 5.1 million, launched in 2000, is still active.

## 2. Rationale for using financial engineering instruments

### *SOP IEC rationale*

The rationale for the SOP IEC, KAI 1.2 SMEs access to finance, is based mainly on the severe undercapitalisation of most SMEs. The document mentioned additional constraints encountered by SMEs, such as: lack of business support services, limited entrepreneurial skills and experience and insufficient knowledge of how to enter markets.

Although the commercial banks improved their targeted services to SMEs, the SOP IEC analysis revealed the lack of business development support provided by the banks to SMEs and a very low exposure to risk. This could explain the fact that 78% of the enterprises were financing their development from their own resources<sup>3</sup>.

As regards the Venture Capital (VC) the SOP IEC highlights the shortage of VC on the market and the reluctance of investors, to invest in this field, due to *unavailability of professional, skilled management teams and limited alternatives on exit*.

The analysis led to the conclusion that the capital markets could not offer accessible financial instruments to Romanian SMEs, to support their development.

A more detailed analysis of the financing gaps concerning SMEs was carried out by the EIF under JEREMIE Initiative in 2007, in order to identify the most effective innovative ways to support SMEs. The study identified four market gaps (details in Annex Table A):

1. Debt financing/guarantees: difficulties for SME to borrow, in particular if new or active in manufacturing.
2. Micro-lending market gap: challenging access to finance through the traditional banking system for many aspiring new/self-employed entrepreneurs.
3. Venture capital market gap: undeveloped early-to-growth stage VC
4. Technology transfer market gap: very little market oriented Research and Development (R&D) in Romania;

More recent studies and evaluations<sup>4</sup> of the Romanian business environment, and the capacity of beneficiaries, particularly SMEs, to implement Structural funds projects, confirm the market gaps and an increasing difficulty to access credit.

### *Equity fund market*

<sup>2</sup> Romanian Government transferred the funds available to the Romania Counter Guarantee Fund, according to the exit Agreement with EC.

<sup>3</sup> Survey conducted 2006 by the National Council of Small and Medium Size Private Enterprise in Romania

<sup>4</sup> Evaluation of ROP 2007 – 2013 priorities and projects addressed to the business environment, March 2011; Evaluation Challenges in the capacity of structural instruments beneficiaries, 2011.

According to the South Eastern Europe's Private Equity Association the equity market, including venture capital, decreased in the last two years, in Romania. In 2011, Romania attracted 50% less private equity than in 2010, when another significant drop was registered. The investments were targeted to specific sectors, and deals with the entrepreneurs encountered difficulties due to the decreased value of their companies. This situation confirms the relevance of hybrid venture capital instrument for the market needs.

#### *FEIs for Urban Development*

Although JESSICA<sup>5</sup> programme has not been implemented yet in Romania, the rationale for FEI addressing urban development has been analysed in the JESSICA Evaluation Study for Brasov Growth Pole. The evaluation concluded that there was a clear demand, and that the public and private sector were very keen on using revolving funds to finance economic development. The study identified sufficient potential projects that could proceed with a pilot JESSICA programme.

#### *FEIs versus grants*

The documents studied and the interviews conducted revealed a general awareness of the potential benefits of using FEIs for SME support.

However, the use of FEIs, instead of grant schemes, encounters a number of difficulties. FEIs and their implementation mechanisms are unfamiliar, and some public bodies may be reluctant to adopt the new mechanism designed to produce results in the long term. The JEREMIE experience showed that setting up the mechanisms for implementing FEIs may involve adjustments of the legislation or financial, regulatory issues, compliance with EU regulations. The implementation of a pilot programme using the new FEIs could make them more acceptable and attractive to future potential beneficiaries.

Our assessment confirmed that grants continue to be perceived as a necessary support measure for SMEs. Grants should be directed to strategic sectors (if they have been identified), specific market segments with low return of investments, high risk or uncertainty, e.g., innovation and technology transfer. The grant schemes, offered indiscriminately to various sectors and target groups, are in danger of distorting competition and obtaining results that have no significant or measurable impact.

According to the officials interviewed the grants should not be directed towards the SMEs "doing badly", but to the SMEs with a high potential "to do really well". The current experience with the implementation of grant schemes shows that the tools for selecting projects are not very effective in distinguishing the two categories.

The main benefit of FEIs is the potential to produce long term results, due to the revolving feature. FEIs implemented by banks, or other financial institutions, are perceived as more business oriented than grants and a filter projects on the basis of business viability criteria. At the same time, the compliance with EU regulations and the necessary flexibility to consider the potential wider benefits for the economy, instead of abiding only to the rigid bank rules, are considered an added challenge.

#### *Costs of FEIs and Grant schemes implementation*

The studies on the administrative costs of the Cohesion policy<sup>6</sup> in Romania highlighted that a significant share of the administrative costs, were incurred for the creation of the implementation

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<sup>5</sup> Joint European Support for Sustainable Investment in City Areas, an initiative of DG Regio.

<sup>6</sup> Study: Regional Governance in the context of globalisation: reviewing governance mechanisms and administrative costs [http://ec.europa.eu/regional\\_policy/sources/docgener/studies/pdf/2010\\_governance.pdf](http://ec.europa.eu/regional_policy/sources/docgener/studies/pdf/2010_governance.pdf)

system of the Structural Instruments, in particular for the 2007-2013 Structural Instruments (SI) cycle, implemented in Romania for the first time. According to the MA for SOP IEC, since the system is functional and significant experience was acquired in the implementation of the grant schemes, the future implementation costs are expected to be lower compared with the current cycle. However, the possible changes of the EU regulations, for the next programming period, could add supplementary costs to adjust the system.

In addition to the management costs with the EIF as Fund Manager<sup>7</sup>, the implementation of FEIs generates further administrative costs with the institutions involved in preparation and implementation. The recent JEREMIE experience shows that the process was not easy, the negotiations for the Funding Agreement between the Romanian Government and EIF took six months, the compliance of the EIF with the EU Regulations was challenging, clarifications and notifications on eligibility or state aid issues are time consuming. There were no studies available, at the time of the research, regarding the administrative costs of FEI implementation in Romania.

The issue of the costs was raised in relation to JESSICA implementation. The absence of a simulation of costs and a clear idea of the future costs of the JESSICA instrument, led to the postponement of project. A clear idea concerning the implementation mechanisms of FEIs, with the associated costs, is essential in the decision making process for the new programming cycle.

### 3. The effectiveness of financial engineering instruments: selected examples

The JEREMIE Romania programme has two financial engineering measures in implementation. While the loan guarantee programme has been operational since 2011, with three financial intermediaries<sup>8</sup> contracted, the risk capital instrument should start operating only in the second quarter of 2012. The analysis of the effectiveness of FEIs is based on the experience acquired to date.

#### *Objectives of loan guarantee programmes*

The objective of the KAI1.2 SMEs access to finance is formulated in rather general terms, in SOP IEC: the establishment of a favourable environment for sustainable development of enterprises (by reducing the constraints in the areas of market failure), improvement in credit access, and creation of innovative financial instruments, etc. More specific objectives are formulated in the Funding Agreement between the Romanian Government and the EIF for JEREMIE Romania, referring to the market gaps that the proposed FEIs should address.

The aim of the loan guarantee programme, the FLPG instrument, is to increase the volume of credit accessed by SMEs. Although the strategy for implementation, part of the Funding Agreement, mentioned that the instruments will in some cases favour specific segments (young and/or innovative SMEs), the implementation mechanism does not achieve this aim. The FLPG Instrument mobilised additional resources from the private capital market, and made them available to the targeted beneficiaries, SMEs. At the end of 2011 a EUR 80.5-million JEREMIE Fund contribution to FEI created a portfolio volume of EUR 402.5 million.

Comparing FLPG with a private loan guarantee fund, the Romanian Loan Guarantee Fund (RLGF), set up in 1993, pursues a similar objective: to increase the volume of finance available to entrepreneurs. However, while FLPG is oriented towards the market gaps, RLGF is more oriented towards “viable

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<sup>7</sup> According to the Government Decision 514/14.05.2008 for approval of the FA between the Romanian Government and the EIF for JEREMIE implementation, the “costs letter” is not published, being classified information according the legislation in force.

<sup>8</sup> At the end of 2011 a third financial beneficiary was contracted

projects". The eligibility rules of FLPG, part of them imposed by the EU regulations, narrow the market to the targeted segments.

RLFG is addressed to a wider market, including enterprises, of any size, entrepreneurs, and other private economic operators. The concern for business viability is also reflected in the pack of additional business support services, flexibility in responding to market needs, cooperation with a large number of banks and diversification of services.

*Operations of the loan guarantee programme.*

At the end of 2011, JEREMIE FLPG Instrument was operational with three selected financial intermediaries.

1. Romanian Commercial Bank with a portfolio volume of EUR 212.5 million, and guarantee cap amount up to EUR 42.5 million.
2. Raiffeisen Bank, with a portfolio volume of EUR 102.5 million, and guarantee cap amount up to EUR 20.5 million.
3. Unicredit Tiriak Bank with a portfolio volume of EUR 87.5 million, and guarantee cap amount up to EUR 17.5 million<sup>9</sup>.

More details on FLPG operations are presented in Annex Table B.

A key operational feature of the JEREMIE FLPG is the "zero cost". Private funds used to charge an application fee, in case of RLGF, EUR 150, and an annual guarantee fee (between 2 and 4.5% of the guarantee, depending on the risk level). The most important "competitor" of JEREMIE FLPG is the National Loan Guarantee Fund for SMEs (NGF<sup>10</sup>), a public fund, which has expanded operations significantly in recent years, including public administration beneficiaries. With 2,400 guarantees contracted during the first quarter of 2012, NGF is perceived successful on the market. NGF is not a "zero cost" scheme but the guarantee fee is low, between 1.5% and 2.5% of the guarantee.

FLPG is perceived more bureaucratic than the private guarantee funds, due to the paperwork specific to EU funding. This means a longer approval procedure and additional administrative burdens. Private funds only require the letter of the partner bank providing the loan, the business plan, and the payment of fees. However, the decision making process is internal in the bank and faster than in the case when an external institution decides the approval of the guarantee. An additional benefit for the final recipients could be a reduced interest rate applicable only for the JEREMIE guaranteed loans.

Although the list of exclusions of eligible sectors is not long, JEREMIE cannot be accessed by all sectors. Private guarantee funds have a competitive advantage; they are accessible to all sectors and all economic operators, not only SMEs. In some cases enterprises of typical SME size, because they are set up by, and linked to, a larger Romanian or foreign company, classify as large enterprises, and are therefore not eligible. It is worth mentioning that, in some cases, the EU eligibility rules are difficult to comprehend by SMEs and operators as well, e.g. "de minimis rule".

The JEREMIE guarantee is limited to EUR 1.5 million, and not more than 80% of the value of the loan, while NGF guarantee amounts to EUR 2.5 million, and the same limit of 80% of the loan value. In RLGF the guarantee limit amounts to 70% of the loan. The FIs have indicated as disadvantages of JEREMIE the non-revolving feature of the working capital facility, and the restrictions regarding the "bullet" reimbursement.

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<sup>9</sup> Operational only starting the second quarter 2012.

<sup>10</sup> Due to the long name in Romanian it is often referred to as National Guarantee Fund (NGF).



*Objectives and operations of the Risk capital instrument*

According to the official documents, the objective of the JEREMIE venture capital instrument is the development of the risk capital investments sector.

According to a KPMG study, carried out for the European Association of Venture Capital<sup>11</sup> in 2009, Romania was one of the less attractive European countries for private equity and venture capital, despite de low rate of tax on profit and income.

The JEREMIE venture capital instrument was designed, as a hybrid venture capital scheme. A selected financial intermediary has to set up a fund, 70% from JEREMIE and the remaining 30% from private investors. The significant public contribution is meant to mobilise private investors' resources, and ensure that the fund reaches a volume, that will make it attractive for fund managers and private investors. In the JEREMIE Romania case, the contribution of EUR 17.5 million would generate a VC fund of at least EUR 25 million.

The scheme can be considered a "happy union" of the public interest and private investors' interest. The public interest is reflected in the eligibility rules, SMEs, and the external benefits beyond the financial return on investment. 20 companies are expected to benefit from this scheme (EUR 35 million allocated). The scheme leaves room for private investors' interests too; commercial principles for the fund manager's payments are included and are related to the fund performance, measured with specific indicators. The JEREMIE fund management costs are agreed on a competitive basis during the selection procedure of the financial intermediaries, as laid down in the EU Regulations<sup>12</sup>. The financial intermediaries can adjust the operations to the market opportunities, by proposing in the selection process, appropriate market segments and financial conditions for operations, however, maintained within the larger framework of the JEREMIE programme.

Flexibility is a differentiating factor between a private and public scheme. The private investors need flexibility in setting the rules. It is difficult to introduce changes in public funding operations in all phases have to comply with the specific EU Regulations, and national legislation. In JEREMIE Romania the lack of flexibility, among others, led to the cancellation of one operation. All operations are subject to verification and audit, and all relevant documents have to be made available to the competent institutions. This requirement is considered an administrative burden by the private operators.

The time aspect also differentiates approaches and operations. Venture capital schemes usually extend over 10 years. As programmes cannot exceed the programming cycle, in the case of a delayed start of FEIs (JEREMIE), only 3-4 years remain for concluding the operations. A solution with asymmetric payments was applied in order to ensure that JEREMIE funds are paid before 2015.

Nevertheless, public participation in a Risk Capital Fund, could inspire confidence and trust among private investors and beneficiaries, to a certain extent making up for the administrative burden created by the EU rules.

For the JEREMIE fund and the MA, the scheme must comply with the programme calendar in order to contract and use the money in the programmed and available time frame, and obtain the expected outputs and results as planned.

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<sup>11</sup><http://www.wall-street.ro/articol/Companii/58760/KPMG-Romania-in-coada-tarilor-din-Europa-la-stimularea-investitiilor-de-private-equity.html>

<sup>12</sup> Art 43. Reg. 1828/2006

*The Managing Authority role: strategy, monitoring and evaluation, control and audit*

As stipulated in the Funding Agreement the MA plays a strategic role in the implementation of the JEREMIE programme; The Investment Committee of the JEREMIE Romania programme, together with the MA, are responsible for revising the strategy of the fund, the investment plan and proposing/approving the necessary changes.

The reporting system of the EIF to the MA is designed to ensure an adequate management of the programme as well as the reporting requirements to the Romanian Government and the European Commission. The main monitoring tools of the MA are quarterly and annual progress reports which should be approved by the MA.

All operational agreements of the JEREMIE programme have to ensure that the audit and control activity is delivered according to the procedures applicable to SOP IEC operations.

*JEREMIE beneficiaries*

The eligible beneficiaries for JEREMIE programme are defined in the Funding Agreement and the state aid/ de minimis aid schemes, issued for the two FEIs implemented.

The eligible beneficiaries are SMEs, with less than 250 employees, turnover less than EUR 50 million and balance sheet total less than EUR 43 million. There are no additional eligibility rules for sectors and applicant/administrator than the ERDF rules. For example, the information fiche for SMEs for the BCR loan guarantee instrument is shown in Annex C.

In the case of FLPG instrument, in addition to the above general eligibility rules, the applicant also have to abide by the “de minimis” rule. The beneficiary is assessed by the bank, using the bank scoring system in order to decide the award of the loan and the guarantee. Since the FLPG instrument covers up to 80% of the loan, the applicant has to be able to cover the remaining 20% according to the bank internal regulations. In case of a high risk beneficiary the guarantee requested could be more than 100 % of the loan.

When using Risk capital instruments, the financial intermediaries propose, as part of their strategies, the target market segments which they will specifically address. However, the selected beneficiaries have to comply with ERDF eligibility rules, as well. Since the operations are planned to start in the second quarter of 2012, there is no experience yet related to the selection of the beneficiaries for the Risk capital instruments.

*FEIs performance*

The expected performance of FEIs in Romania, specifically the JEREMIE Romania programme, is defined by the SOP IEC, KAI 1.2 SMEs access to finance. Further details are given by the implementation documents: the FA between the Romanian Government and the EIF, and the state aid/ de minimis aid schemes.

According to the above mentioned documents the indicators are structured as follows:

Three output indicators (relating to the operational objectives of the scheme) are defined:

1. SMEs supported through Loan guarantee funds; target value: 200 SMEs<sup>13</sup>, by 2015.
2. SMEs supported through Risk capital funds; target value: 20 SMEs<sup>14</sup>, by 2015.

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<sup>13</sup> According to the “de minimis” state aid scheme for loan guarantee instrument

<sup>14</sup> According to the state aid scheme for the risk capital instrument

3. Number of guarantee and Risk capital operations; target value: approx. 10 by 2015.

At the programme level, only “the financial engineering instruments” are reported as an output program indicator.

The SOP IEC documents do not define results and impact indicators. However, the first two indicators listed above (the number of SMEs supported), could be also considered result indicators rather than only output indicators.

According to the FA<sup>15</sup>, the EIF is responsible for the “complete utilisation, by the SMEs” of the funds allocated by the SOP IEC. However, the EIF cannot be held accountable for the financial performance of the fund and the operations<sup>16</sup>.

The FEIs performance is measured through the monitoring and evaluation system of the SOP IEC. There is a Funding Agreement specifying the requirements. The quarterly and annual progress reports are the main tools and include, among other information, the following quantitative data:

1. Number of funds /per type (Guarantee, Equity, Risk Capital)
2. Number of SMEs beneficiaries per type of FEI
3. Amount mobilised by the JEREMIE Holding Fund
4. Total volume of the portfolios and the private resources mobilised

At the end of 2011 the EIF reported the following achievements of the JEREMIE Romania programme:

1. 4 financial engineering funds supported: 3 loan guarantee funds<sup>17</sup> and 1 risk capital fund
2. 142 SMEs supported through the guarantee instruments (FLPG)
3. Volume of loans generated by FLPG: EUR 11.7 million;
4. JEREMIE HF amount contracted for FLPG instrument: EUR 80.5 million:
5. Total additional resources committed at the level of the final recipients for FLPG<sup>18</sup>: EUR 322 million
6. Total portfolio volume of FLPG instrument: EUR 402.5 million
7. 0 SMEs supported through risk capital instruments<sup>19</sup>
8. JEREMIE HF amount contracted for Risk capital instrument: EUR 17.5 million

The targets, set for the indicators on SME support, are relatively modest, compared to other similar operations such as NGF. However, the target of 220 SMEs, is feasible, considering that 142 SMEs have already been reached. The number of funds supported – as an output programme indicator, with a target value of “approx.10”, is difficult to achieved, considering that the total allocation of EUR 100 million was contracted for four operations.

It might be advisable, to identify result indicators and additional indicators related to the operations of each instrument, observing how the support is channelled to specific segments of SMEs, according to the market gaps identified.

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<sup>15</sup> Article 12.2.1. of the FA

<sup>16</sup> Article 13.2. of the FA

<sup>17</sup> Only two guarantee funds were operational at the end of 2011 with a total portfolio of EUR 315 million, the third guarantee fund was contracted and started the operations in March 2012 and the risk capital fund was expected to start in second quarter of 2012

<sup>18</sup> Additional resources mobilised for RISK capital instrument not reported.

<sup>19</sup> At 31 December 2011, no operation was active on Risk Capital Instrument

#### 4. Main problems in using financial engineering instruments

JEREMIE Romania had a late and difficult start. FEIs and their specific mechanisms are not very well known,

The FEIs with the support of the Cohesion policy are new to the Romanian administration. The pre-accession experiences were very few, on a small regional scale, and isolated rather than integrated in a national policy.

The JEREMIE programme implementation encountered a number of difficulties related to various regulatory issues: provisioning and capital relief regulations. The solutions found with the financial intermediaries, EIF, MA, and the regulator, have led to amendments of the operational agreements.

FLPG implementation dealt with problems generated by uncertain interpretation of the eligibility rules, the applicability of the Romanian legislation on SF eligibility rules, concerning VAT and land acquisition; the process of clarification took DG Regio several months. In the meantime, the financial intermediaries were advised to adopt a conservative position with a rather narrow interpretation of eligibility. Our research revealed the FIs need support from EIF which could facilitate learning from other countries' experience as regards implementation of FEIs funded by ERDF.

The Financial Intermediaries for FLPG highlighted a number of operational difficulties linked to the verification of the eligibility criteria, i.e., the "de minimis" rule, the type of enterprise in the case of international groups, the NACE classification in the context of ERDF sectors and activities exclusions.

In the case of the risk capital instruments, the negotiation process with the private investors proved difficult. The specific requirements of the investor, unacceptable within the framework of the JEREMIE program, led to the cancellation of the agreement with one of the financial intermediaries, who could not mobilise the required private resources in the expected timeframe. In order to ensure spending according to schedule, the JEREMIE fund (in agreement with the MA) decided to reallocate the sum resulting from the cancellation of the contract to the FLPG Instrument which is characterised by a good spending potential.

The beneficiaries of the loan guarantee instrument find the eligibility rules limiting, mainly the VAT and the 10% eligibility condition for land acquisition. The administrative burden created by the number of documents requested, as well as the control and verifications, to which they are subjected according the EU rules, are perceived by SMES as weaknesses of the JEREMIE programme.

The economic crisis affected the operations of the instruments; the demand for loans decreased, the Romanian VC market for private investors is less attractive, because there are fewer opportunities for business development. The business environment is perceived, by investors, less favourable than in other European countries.

The willingness and capacity of the main actors to implement FEIs is essential for a smooth and efficient process, however, the JESSICA experience (Growth Pole Brasov), proved that the actors are still not ready to implement urban development funds. They have to understand and accept the challenges of change, and the relative benefits compared to grant schemes.

#### 5. Evaluations of financial engineering instruments

JEREMIE Romania programme was subject of evaluation in the first ongoing evaluation of the SOP IEC. The evaluation, finalised in June 2010, pointed out that the JEREMIE programme was still at a very early stage, and urged an ad-hoc evaluation, in order to accelerate implementation.

The JEREMIE evaluation was also recommended in the Monitoring Committee of the SOP IEC, meeting, held on 24 November 2011, as part of the SOPIEC multiannual evaluation plan. The evaluation is meant to provide additional knowledge concerning the implementation of FEIs in Romania, keeping in mind the increased importance given to such instruments in the next programming period.

According to the MA for SOP IEC, the JEREMIE evaluation was postponed to 2012, in order to wait for the FEI risk capital instrument to become operational. The evaluation will be focused on EIF management and the results achieved to date.

## 6. Concluding remarks

The JEREMIE Romania programme is the first FEI, with Structural Funds support, implemented in Romania. Lessons learnt from JEREMIE implementation may be very important for extending FEIs in the Cohesion policy programmes.

FEIs have a high potential to complement the current instruments, and enhance the support to enterprises, and regions. Compared with grant schemes, FEIs ensure the recycling of funds and a mechanism capable to deliver results over a longer period of time.

By involving the financial institutions in the support delivery mechanisms, FEIs could apply more effective business oriented filters in the selection of the beneficiaries. However, the financial institutions are less flexible in integrating in their practice the Cohesion policy concepts and rules, the wider objectives, beyond the financial performance of the specific operation.

Grant schemes continue to be needed in Romania. The experience of the current SI could lead to improvements in the grant schemes, focussing on a clear strategic sectorial focus, identification of market segments, where the investment return and the level of risk, require the non-refundable grants, instead of FEIs.

Grants are very popular in Romania. A large amount of knowledge has been acquired in many institutions and organisations. Some beneficiaries and institutions involved in the implementation of Cohesion policy may be reluctant to accept a massive replacement of grants with FEIs, unless they perceive the relevant benefits and accept the cost of the change.

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## Interviews

Mrs Ioana Ciocoiu - Authority for Coordination of Structural Instruments, Programming Directorate

Mrs Cătălina Melița – Managing Authority Sectorial Operational Programme, Increase of Economic Competitiveness

Mr Sorin Maxim – Regional Development Agency West, Intermediate Body for Regional Operational Programme

Mr Mihail Vestea – Regional Development Agency West, Growth Pole Brasov

Mrs Sanda Popescu – EXIMBANK, chief economist

Mr Florin Ilie- ING Bank, Capital Markets Directorate

Mrs Cornelia Bradean – Romanian Commercial Bank, Deva Branch, Retail Director

Ms Mirela Musat – Raiffeisen Bank, Financial Intermediary for guarantee instruments

Mr Marius Radu - UniCredit Tiriac Bank –Vicepresident Head of EU Funds Financing<sup>20</sup>

## Annex

**Annex Table A: Summary of the market gaps**

	Observed market gap	Proposed Instrument
Debt financing/guarantees	Difficulties for SME to borrow, in particular if new or active in manufacturing.	Reinforce the national guarantee system through EUR 120-150 million targeted injection to stimulate lending to SMEs.
Micro-lending	Gaining access to finance through the traditional banking system is challenging for many aspiring new/self-employed entrepreneurs.	Support of micro-finance institutions by deploying c. EUR 40 million via direct funding or a specific guarantee instrument.
Venture capital	Early to development stage VC is under-developed.	Fund-of-fund of ca. EUR100 million to support VC initiatives in the country.
Technology transfer	R&D in Romania is very seldom directed to create market-oriented intellectual property	Creation of a EUR 30 million facility to a support technology transfer scheme to stimulate the production of “monetisable” intellectual property and finance pre-seed R&D projects with the potential to lead to a viable spinout business

*Source: Executive Summaries of Evaluations Studies on SME Access to Finance in Member States/Regions carried out by EIF in the context of the JEREMIE, 2009;*

<sup>20</sup> Opinions from Raiffeisen Bank and UniCredit Tiriac Bank have been received in written based on a questionnaire sent to the three FI for the FLPG operations

**Annex Table B: Stage of implementation of JEREMIE programme at 31.12.2011**

Operation	First Loss Portfolio Guarantee (FLPG) Operation	Date of the agreement	Start of Implementation	JEREMIE contribution (EUR million)	Portfolio Volume (EUR million)
Financial Intermediary	Banca Comerciala Romana	30/12/2010	March 2011	42.5	212.5
Financial Intermediary	Raiffeisen Bank Romania	30/12/2010	April 2011	20,5	102.5
Financial Intermediary	Unicredit Tiriac Bank	19/12/2011	March 2012	17.5	87.5
<b>Total allocated for FLPG instrument</b>				80.5	402.5

Operation	Risk capital Operation	Date of the approval	Start of Implementation	JEREMIE contribution (EUR million)	Comments
Financial Intermediary	Ascenta Operation	1/10/2010	cancelled	17.5	reallocated to FLPG
Financial Intermediary	Catalyst Operation	18/02/2011	2nd quarter of 2012	17.5	JEREMIE contribution cannot exceed 70% of the operation fund
<b>Total allocated for risk capital instrument</b>				17.5	

Total contracted with financial intermediaries from JEREMIE fund (EUR million)	98
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Source: JEREMIE Annual Progress Report 2011



## **Annex 1: Romanian Commercial Bank – Presentation fiche of the JEREMIE Loan Guarantee Scheme**

*Loan for investments / working capital / stocks with JEREMIE guarantee*

Through BCR a company could benefit from investment loans/ loans for working capital / stocks, granted from BCR sources and offered free of charge with JEREMIE guarantee of 80% of the loan value.

*Eligible SMEs:*

Loans are granted to SMEs (including start-ups) which fulfil the specific criteria for selection, in order to finance the activities under the eligible sectors (excepting mainly the sectors from agriculture, fishing, forestry as well as the projects which already take the benefit of other non-reimbursable financing), carried out in Romania, such as:

- a) investments for tangible and intangible assets
- b) working capital related to the development or expansion of the activity

Currency: RON / EUR

Maximum amount: EUR 1.9 million (respectively EUR 0.9 million if the activity is from road transport domain)

Term: minimum 12 months, maximum 6 years

*Guarantees:*

- -80% of the loan value represents the guarantee granted by BCR on the name of the European Investment Fund (maximum EUR 1.5 million) under JEREMIE Initiative.
- -other guarantees, according to the specific internal regulations in force

Other characteristics of the JEREMIE guarantee:

- JEREMIE guarantee is a portfolio guarantee granted under “The transparent scheme of minimis aid in the form of loans portfolio guarantees, as part of the implementation of JEREMIE Initiative in Romania”, the scheme approved by the Order no. 1.338/2010 issued by the Ministry of Economy, Trade and Business Environment, the de minimis aid provider being the Ministry of Economy, Trade and Business Environment, through the Management Authority of SOP ECC.
- JEREMIE Initiative is financed from EU structural funds, respectively under the European Regional Development Fund, through SOP ECC, Priority Axe 1 “An innovative and eco-efficient production system” the major field of intervention 1.2 “SME access to financing”.
- JEREMIE guarantee is subject to the “De minimis” aids rules and does not require the payment of any guarantee commission.

*Documents:*

Application form for a financing with JEREMIE guarantee

Declaration under its own responsibility that the company is included in the SMEs category and meets the criteria requested by Order no. 1338 / 2010

Declaration under its own responsibility regarding the de minimis aid and not being in the category of “distressed companies”

Declaration under its own responsibility about being / not being included in the restricted and excluded sectors

Certificate issued by the Trade Register, Certificate issued by the Insolvency Bulletin, Tax Certificate, Criminal Record Certificate

Economic and financial situations (balance sheet etc.)

Other documents requested by the bank (feasibility study, business plan etc.)

*Advantages:*

- 0 guarantee commission
- preferential loan conditions compared to standard loan conditions, respectively reduced costs (interest rates, commissions)
- reduced requirements on the volume of additional guarantees

This funding is supported through a sectoral operational program co-financed with EU Structural Funds through JEREMIE initiative. Specifically, JEREMIE initiative is implemented in Romania through the Sectorial Operational Program „Increasing Economic Competitiveness”, with funds provided by the European Regional Development Fund.