Africa Team & Energy and Infrastructures Focus Team

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THE EUROPEAN FUND FOR SUSTAINABLE DEVELOPMENT AND THE EFSD GUARANTEE

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1 INTRODUCTION

With the purpose of creating new investment support measures in European neighbourhood countries and in Africa, on 26 September 2017 the European Parliament and the Council of the European Union, with Regulation 2017/1601 (**Regulation 1601**), have established the European Fund for Sustainable Development (**EFSD**), the EFSD Guarantee and the EFSD Guarantee Fund.

In the same framework, the European Commission (**Commission**) allocated EUR 4.1 billion to this initiative: EUR 1.5 billion to the EFSD Guarantee and EUR 2.6 billion to the African Investment Facility (AfIF) and the Neighbourhood Investment Facility (NIF). The Commission estimates that these funds will generate over EUR 44 billion by 2020.

2 EFSD: OBJECTIVES AND STRUCTURE

The paramount objectives of the EFSD are (i) to enable investors and private businesses to more effectively contribute to the sustainable development of partner countries (in line with EU development and neighbourhood policies), through guarantees to support investment and (ii) to involve the private sector in the sustainable development activities of EU partner countries.

Other EFSD objectives include: a) fostering decent job creation, green and inclusive growth, gender equality and the empowerment of women and young people; b) strengthening the rule of law, good governance and human rights; and c) implementing the Paris Agreement on climate change by targeting investments in sectors that aim to reduce and mitigate climate change.

The EFSD structure is based on 2 regional investment platforms:

a) the Africa regional investment platform; and
b) the EU neighbourhood regional investment platform.

The EFSD fund is managed by the Commission in close cooperation with the European Investment Bank (EIB) with the support of a strategic board that advises the Commission on strategic direction and investment priorities. On an operational level, the Commission (after consulting the strategic and operational boards and informing the European Parliament and the Council) sets up dedicated investment windows, for which requests for financial support to the EFSD can be submitted. These investment windows can be dedicated to specific regions, specific partner countries or both, specific sectors, or for specific projects, specific categories of final beneficiaries, or both.

Once the investment windows are chosen, the individual financial support requests must be submitted to the Commission, which assesses whether the eligibility criteria under Regulation 1601 are met (please see section 4.1 below for more details).

3 THE REGIONAL INVESTMENT PLATFORM FOR AFRICA

The Africa investment platform (**AIP**) was originally created in 2015 as the African Investment Facility and was renamed in 2017 to become the EFSD's operational instrument for the African region.

The main purpose of the AIP is to support sustainable growth in Africa by fostering investments that will have a positive impact on the region's socio-economic development. In particular, according to Regulation 1601, a significant share of the EFSD Guarantee granted through the AIP must be allocated to fragile and conflict-affected countries, landlocked countries and least developed countries.

Investments have to be focused on infrastructure-related sectors – such as transport, communication, water, energy and agriculture – and used to support private sector development, particularly SMEs. In particular, the beneficiaries can be either:

a) partner countries, either directly or indirectly through their central, regional and local administrations or public or semi-public institutions; and

b) the private sector, particularly households and SMEs.

4 THE EFSD GUARANTEE

The EFSD Guarantee is an irrevocable and unconditional first demand guarantee that can be used to cover the risks concerning the following investment and financing instruments:

a) loans, including local currency loans;
b) guarantees;
c) counter-guarantees;
d) capital market instruments; and
e) any other form of funding or credit enhancement, insurance, and equity or quasi-equity participations.

The EFSD Guarantee can be used only if the Commission and the "eligible counterparts" (**Eligible Counterparts** – please see section 4.2 below for more details) enter into guarantee agreements, provided that the Eligible Counterparts meet both objective and subjective eligibility conditions under Regulation 1601.

The investment period during which the Commission can enter into EFSD Guarantee-related agreements with Eligible Counterparts to support financing and investment operations expires on 31 December 2020.

Eligible Counterparts have then four years from entering into an EFSD Guarantee agreement to enter into agreements with co-financing private sector partners, financial intermediaries or final beneficiaries.

Industrial investors that are not Eligible Counterparts but invest in an investment window identified by the Commission and that meet the criteria under Regulation 1601 can access the EFSD Guarantee system indirectly through Eligible Counterparts, by entering into an agreement to receive loans, including local currency loans, guarantees, counter-guarantees, capital market instruments, and other credit or business risk supporting measures offered by the Eligible Counterpart, which in turn benefit from the EFSD Guarantee.

4.1 Objective eligibility criteria to access the EFSD Guarantee

Only financing and investment operations that pursue specific objectives can benefit from the support of EFSD Guarantee, including (among others):

a) contributing to sustainable development in its economic, social and environmental dimensions, and to the implementation of the 2030 Agenda[1] and, where appropriate, the European Neighbourhood Policy, with a particular focus on the eradication of poverty, the creation of economic opportunities and promoting in particular gender equality and the empowerment of women and young people;
b) contributing to the implementation of the Union's migration policy;
c) strengthening socioeconomic sectors and areas and related public and private infrastructure, including renewable and sustainable energy, water and waste management, transport, information and communications technologies, as well as environment, sustainable use of natural resources, sustainable agriculture and blue growth, social infrastructure, health, and human capital, in order to improve the socioeconomic environment;
d) providing finance and support to private and cooperative sector development, with a particular focus on local companies and micro, small and medium-sized enterprises, while addressing market failures, limiting market distortions and encouraging the contribution of European companies to the EFSD objectives;
e) contributing to climate action and environmental protection and management, thus producing climate co-benefits, allocating at least 28% of the financing to investments that contribute to climate action, renewable energy and resource efficiency;
f) providing financial instruments, which may be denominated in the local currency of the partner country concerned, including first loss guarantees to portfolios, guarantees to private sector projects such as loan guarantees for small and medium-sized enterprises, and guarantees for specific risks for infrastructure projects and other risk capital; and
g) leveraging private sector financing, with a particular focus on micro, small and medium-sized enterprises.

In order to benefit of the EFSD Guarantee, the financing and investment operations must also comply with the "additionality principle", *i.e.*, the operations would not be feasible - or, although feasible, would not be

[1] Please see footnote 1.

able to achieve the same results - without the support of the EFSD Guarantee.

4.2 Subjective eligibility criteria to access the EFSD Guarantee: Eligible Counterparts

Under Regulation 1601, only entities that meet certain prerequisite (so called Eligible Counterparts can benefit from the EFSD Guarantee, *i.e.*, investors and financial institutions that fall under the following categories:

a) the EIB and the European Investment Fund;
b) public law bodies;
c) international organisations and their agencies;
d) bodies governed by private law with a public service mission to the extent that they provide adequate financial guarantees;
e) bodies governed by the private law of a Member State that provide adequate financial guarantees, by way of derogation from point (vii) of point (c) of Art. 58(1) of Regulation (EU, *Euratom*) No. 966/2012[2]; and
f) bodies governed by the private law of a partner country that provide adequate financial guarantees, by way of derogation from point (vii) of point (c) of Art. 58(1) of Regulation (EU, *Euratom*) No. 966/2012[3].

In the case of bodies governed by the private law of an EU member state or an EU partner country, preference must be given to those that disclose information relating to environment, social and corporate governance criteria.

In any event, all Eligible Counterparts must comply with Art. 60 of Regulation (EU, *Euratom*) No. 966/2012, specifically:

a) comply with the principles of sound financial management, transparency and non-discrimination; and
b) use instruments that ensure the EU's control over the management and use of its own funds, duly taking into account, among other things, the nature of the roles entrusted to Eligible Counterparts, the related amounts and the financial risks assumed.

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[2] Bodies governed by the private law of an EU member state that are entrusted with implementing a public-private partnership and that provide adequate financial guarantees.

[3] *Ibid.*

Moreover, to protect the EU's financial interests, Eligible Counterparts must:

a) set up and ensure the functioning of an effective and efficient internal control system;
b) use an accounting system that timely provides accurate, complete and reliable information;
c) be subject to an independent external audit, performed in accordance with internationally accepted auditing standards by an audit service functionally independent of the entity or person concerned;
d) apply appropriate rules and procedures for providing financing from Union funds through grants, procurement and financial instruments;
e) ensure, in accordance with Art. 35(2) of Regulation (EU, *Euratom*) No. 966/2012, the ex-post publication of information on recipients; and
f) ensure reasonable protection of personal data, as required by Directive 95/46/EC and Regulation (EC) No. 45/2001.

5 STATUS OF EFSD IMPLEMENTATION

As of today, based on the documentation available on the Commission's website[4], the following five investment windows have been approved:

a) Sustainable Energy and Connectivity: to attract investment in renewable energy, energy efficiency and transport;
b) Micro, Small and Medium-sized Enterprises (MSMEs) Financing: to improve MSMEs' access to finance;
c) Sustainable Agriculture, Rural Entrepreneurs and Agribusiness: to provide better access to finance for smallholders, cooperatives and agribusiness MSMEs, thus allowing them to address food security issues;
d) Sustainable Cities: to mobilise investment in the sustainable urban development of municipal infrastructure, including urban mobility, water, sanitation, waste management and renewable energy services; and
e) Digital for Development: to create decent jobs and innovative

[4] Press release of 23 November 2017.

digital solutions, particularly those that address local social needs and financial inclusion.

Furthermore, the European Commission has announced that its next step will be inviting Eligible Counterparts to submit proposals for investment programmes that fall under one of the five investment windows.

To date[5], pillar-assessed Eligible Counterparts selected by the Commission for having passed the "pillar assessment" are mainly:

a) financial institutions, such as the EIB and the European Bank for Development and Restructuring (EBRD);
b) bilateral development banks in EU member states, such as the Cassa Depositi e Prestiti (CDP), Agence française de développement (AFD), Kreditanstalt für Wiederaufbau (KfW) and Agencia Española de Cooperación Internacional para el Desarrollo (AECID);
c) European development finance institutions, such as Promotion et participation pour la coopération économique (Proparco), Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden N.V. (FMO), Deutsche Investitions- und Entwicklungsgesellschaft (DEG) and Compañía Española de Financiación del Desarroll (COFIDES); and
d) other regional and multilateral development banks, such as the African Development Bank (AfDB).

The Commission is expected to sign the first agreements with the above financial institutions in the first half of this year[6].

Subsequently, businesses and organisations interested in benefitting from the EFSD Guarantee (and the other EIP supporting measures) can directly submit their project proposals to pillar-assessed financial institutions.

Alternatively, project proposals can be submitted directly to the EIP secretariat, which will put the business in touch with the Eligible Counterpart that manages the relevant investment window[7]. In that case, if the

[5] Q&A of 23 November 2017.

[6] Press release of 23 November 2017.

[7] Q&A of 23 November 2017.

Eligible Counterpart rejects the project proposal, it must notify the EIP secretariat accordingly and justify its decision.

6 CONCLUSION

Businesses, bodies and organisations (be they financial or otherwise) that intend to benefit from the supporting measures under Regulation 1601 and, specifically, from the EFSD Guarantee can opt for one of the following alternatives:

a) Investors that meet the requirements described in section 4.2 (*Subjective eligibility criteria to access the EFSD Guarantee: Eligible Counterparts*) above can undergo the pillar assessment to be qualified as Eligible Counterparts. Once qualified, they may enter into the EFSD guarantee agreements with the Commission and, consequently, be entrusted with an investment window already identified or that may be identified by the Commission.

b) Investors that do not meet the requirements described in section 4.2 (*Subjective eligibility criteria to access the EFSD Guarantee: Eligible Counterparts*) above or that, in any case, do not wish to be qualified as Eligible Counterparts can submit investment projects to an Eligible Counterpart (directly or through the EIP secretariat[8]) that has already entered into a guarantee agreement with the Commission, to thus obtain loans, including local currency loans, guarantees, counter-guarantees, capital market instruments, and other credit or business risk supporting measures offered by the Eligible Counterpart and supported by the EFSD Guarantee.

[8] The contact details are as follows:
Address: Secretariat of the External Investment Plan
European Commission
41, rue de la Loi/Wetstraat, 1040 Bruxelles/Brussels, Belgium
Email: EC-EIP-EFSD-SECRETARIAT@ec.europa.eu

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