

Guarantee Fund for external actions. Codification

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The Commission presents a comprehensive report on the functioning of the Guarantee Fund.

The Guarantee Fund for external actions was established by Council Regulation (EC, Euratom) No 2728/94 in order to shield the Union budget in the event of any default by the beneficiaries of loans granted or guaranteed by the EU. The Fund regulation was amended three times and is currently operating under Council Regulation (EC, Euratom) No 480/2009. Three reviews of the functioning of the Fund took place in 1998, 2003 and 2006. Further to the last review in 2006, a new provisioning mechanism was implemented which entered into force in 2007. An Inter-institutional agreement between the Council and the Commission concluded that a full analysis of the new provisioning mechanism be provided. An evaluation of the Guarantee Fund was commissioned by the Commission in September 2009 with an external consulting company in order to assess the functioning of the new provisioning mechanism and the different parameters of the Guarantee Fund particularly the 9% provisioning target rate.

The **main findings** of the external evaluation are as follows:

- the Fund is an effective and efficient mechanism for provisioning for the risks associated with EU's external lending actions;
- the costs of operating the Fund are modest in relation to the budgetary protection and stability offered by the Fund;
- the current management methods for the Fund are working effectively and are fit for purpose;
- the 9% provision target rate is at an appropriate level and provides a comfortable buffer against loss. Even under an accelerated scenario (a type of default as yet not observed with EU lending), the quantitative assessment indicates that a one in twenty year loss could potentially be provided for;
- the provisioning mechanism takes into account sufficiently well the risk profile of the Fund. Given the unlikelihood of the Fund breaching either the 80 % or 70% triggers, the current mechanism does allow satisfactorily for the associated missed loan payment risks.

As regards the adequacy of budgetary resources foreseen for the Fund, the conclusions of the evaluation are that:

- the payments to the Fund that are due to losses are capped by the smoothing mechanism at EUR 100 million. The modelling results suggest that the smoothing mechanism and the EUR 100 million limit are appropriate;
- the payments to the Fund that arise from additional disbursements are projected to rise above the current annual budget allocation of EUR 200 million.

The **main recommendations** are as follows:

- the Fund should continue to cover the external lending operations of the EU;
- the target rate of the Fund should be maintained at 9%; although it should be reviewed from time to time;
- in the next financial framework, the budgetary resources foreseen for the Fund should better reflect the expected profile of provisioning needs. Accordingly, it would be prudent to increase the annual budget allocation to between EUR 250-300 million;
- further analysis should be carried out to determine whether the same quality of portfolio management services could be achieved by the Commission (as compared to EIB) at a lower cost (in relation to management fees paid to EIB).

In the light of the evaluation, **the report concludes that the Guarantee Fund in its present setting functions well** and that there is at present no need to change the legal base of the Fund or any of the Fund's parameters:

- the new provisioning mechanism has delivered the promised improvement in the budgetary process with a provisioning based on the observed net-disbursements. This has resulted in an improved budgetary process for provisioning the Fund;
- a thorough quantitative analysis of the risk covered by the Fund and the Fund's 9% target rate has shown that this target rate and the other main parameters of the Fund are appropriate. The Commission therefore does not see a need to change the target rate or other Fund parameters. Nevertheless these parameters should be reviewed from time to time in order to consider if they continue to take sufficiently into account the risk profile borne by the Fund. Such a review will be presented in the context of the next comprehensive report on the functioning of the Fund due in 2013;
- under the present financial framework, the total budgetary resources foreseen for the Fund are appropriate however improvements exist regarding the profile of the provisioning needs of the Fund. These should be implemented in the planning of the post 2013.