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European Mutual Guarantee Association¹*

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AECM MEMBERS' ANNUAL REPORTS 2003

A survey of the activity and performances of guarantee schemes dedicated to agricultural and rural businesses.

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As usual, you are invited to circulate this material to your key staff members and your network. Your comments will be welcome. Other members will be illustrated in a next edition.

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RURAL CREDIT GUARANTEE FOUNDATION AVHGA - HUNGARY

Mission Statement

AVHGA is an autonomous foundation created with the special purpose to support by its guarantee the access to credit for Hungarian agricultural and rural businesses. It is managed by a “curatorium” composed of 3 delegates from Ministries, 1 of the National Bank, 5 of banks and of 8 entrepreneurs.

Partnerships of AVHGA

- The Hungarian Government plays a main part as provider of several supports : it completes the SME guarantee premium by a complementary subsidy ; it intervenes as a automatic counter-guarantor (70%) in the payment of losses and it exercises a control on the activity ; finally it gives the legal background to the activity (supervision, competition rules...). Public authorities contributed by 93% in the equity
- Banks are partners in the Foundation’s equity (+/- 7%) and are the lenders of guaranteed credits (more than 10 banks and local networks of saving banks).
- SME circles form the majority in the decision bodies and are by such deeply involved in the management of the scheme.
- EU PHARE programme allocated a start risk Fund.

Facts about 2003

- Hungarian agriculture faced extreme natural conditions (frost and drought affected 94.000 farms. They reported a total damage of €145 million which was partially compensated by a special distress non-refundable aid from the government (€38 million).

From another part, a main trend of the Hungarian agricultural sector was its modernisation : the AVHGA report cited a number of 20.000 undertakings having invested €458 million in machinery, 190 million in new constructions and 76 million in new plantations (vineyards and orchards).

The impact of EU accession became clearly noticeable : farmers assessed their competitive position and moved in the right direction. State subsidy supported their action and a number of producers organisations and sales cooperatives were formed.

- AVHGA modernised its activity and products:

- Non-agricultural guarantees , which were specified on a particular file, were treated under the EU “de minimis” competition rules . The Foundation is requested to notify the state aid amount which is contented in each operation and the beneficiary is requested to retain the notification and to produce it upon a audit. 29% of the 2003 activity was affected by State aid and the average amount of State Aid of the Foundation was calculated at 2,6%..
- The 90% guarantee percentage was abolished in favour of a 80% credit protection
- “Integrators” (large commercial undertakings which sign production contracts with farmers and commit to buy their crops) were given a better access to guarantee : 11 facility conventions were signed with them , assisting the credit operations of 240 small businesses.
- The guarantee fee was increased by 20% on average, varying between 0,25% and 3,2% according to the credit maturity and amount.
- Information technology developments in AVHGA management systems allowed to create a direct link with bank branches through the credit institution headquarter and 100 units were made active.

Some 2003 data

The HUF / EUR exchange rate used in this report is HUF 262,23 for €1. To be noted a depreciation of the national currency which affect the comparison of data with 2002.

Guarantees issued in 2003 .

2003 was a record year with 3.064 guarantees issued for a total of 30,3 billion HUF / €15.550.000. Underlying loans amounted to €192,5 million (HUF 50,5 billion), which is 65% more than the previous year.

The rate of rejected applications was 4,3%.

The average guarantee amount was €37.753

56% of the credits guaranteed by the Foundation received some kind of support (national subsidy, Sapard, EU)

Breakdowns

- 40% of the value was for capital replenishment (loans with a maturity of more than 1 year dedicated to working capital reinforcement) / 31% for credits < 1 year / 28% for credit transactions > 1 year and 1% for technical performance operations.
- Limited liability Cies, sole proprietors and traditional farmers were the primary beneficiaries, indicating the target of small firms. This is confirmed by the beneficiaries per staff number : 2.226 deals benefited to businesses with less than 10 employees (45% in value). But also 255 medium-sized enterprises (>50 employees) were granted guarantees (23% of the granted value)
- The sectorial distribution shows a declining importance for rural development to the profit of the agricultural sector.
- The average maturity of the whole portfolio was 3,57 years compared to 2,3 years in 2002 : Longer durations of credit were used and the majority of transactions were characterised by a 5-6 years of duration, while credits up to 15 years appeared in the portfolio.

Guarantee portfolio

The outstanding guarantee portfolio was €147.914.000 by the end of 2003.

AVHGA's responsible own Funds including an annual retained profit of €6 million, the equity base reached €46.159.000 (49.921.000, provision included)

Defaults

Claims dropped again (3rd consecutive year) in number and in amounts. More than half of claimed guarantees were concentrated in sectors outside agriculture and hit mainly operations granted in 1999-2000.

HUF 497 million (€1895.280) guarantees were claimed / 326 million were recovered by systems of counter-guarantees and 191 million were recovered on the main debtor (+31,5%) Taking into account the State counter-guarantee, a 82% of the initial loss can be recovered.

Compared with the outstanding, the gross rate of losses was 1,48% and the net rate was 0,267%.

Voluntary policies were put in place to improve recovery actions on borrower's assets.

View on the future

EU accession is particularly relevant for the Foundation, with special features on

- The extension of the SME definition : two steps will make it fully compliant with EU definition by the end of 2005. The potential market of the Foundation will be enlarged to new groups of businesses.
- EU State Aid rules will enter in force with a renewal of definitions : in particular, "rural business" will be retracted to a lower number of sectors.
- Improving the ICT (hard- and software) of the Foundation remains a priority.
- New parameters defining the outstanding commitments capacity and relevant own funds are to be further defined. The threshold of HUF 100 billion in accordance with the Budget Act of 2004 should be discussed. Indeed, it is forbidden by law that the portfolio of AVHGA should exceed €28 million and the short term anticipations are higher.

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THE RURAL CREDIT GUARANTEE FUND - ROMANIA

Mission Statement

The RCGF was set up in Feb. 1994 as a joint stock company following the negotiations between the EU PHARE programme and the Romanian Ministry of Agriculture.

The scope of activity is to grant guarantees to commercial banks for loans issued to agricultural producers and processors of agri-food products. The aims of the fund are

* to contribute to a soft transition of Romanian agriculture to market economy through a process of privatisation and modernisation

* to improve community infrastructure in rural areas

* to facilitate access to finance for agri-food industry regarding their production means, inventories and working capital needs.

Basic parameters of the guarantee are :

- Max guarantee amount : € Million
- Max guarantee coverage : 50% of short term loans and 70% of medium-long term ones

Partnerships of the Fund

- Banks, in the number of 5 as shareholders of the Fund (99,95% of the equity capital), and in the number of 11 as users of the guarantee facility. Romanian Commercial Bank was the main player. Special relationship was extended to the Microcredit Foundation Economic Development Center (111 files approved in 2003 for a small amount in all).
- Farms and rural SMEs as beneficiaries of the guarantee all over the country and their representative organisations as discussion partners for the dissemination of the Fund
- The Romanian Government as the Ministry of Agriculture has a symbolic part in the capital (0,05%) and as it provides a partial protection of the losses in some files (Gov. decisions 356/1993 and 567/1996).
- The EU "PHARE" which granted a contribution of € Million as a risk fund for the establishment of RCGF and which continues to have an administrative follow-up regarding the usage made of the subsidy.
RCGF is as well involved in the implementation of EU SAPARD supported projects.

Regulations surrounding the scheme

- Law 31/1990 as base of the setting-up of the Fund
- There is still no supervisory framework to Romanian Guarantee schemes. As a result, the Fund's protection is not recognized by the Banking Control Authorities and the provisions made by the Fund must be duplicated by the Bank's own provisions. This plays as a severe obstacle against the expansion of the Romanian Guarantee Schemes.

Some facts about 2003.

- The main reforms achieved in 2002 led to more attractiveness of the Fund's action and allowed the signature of general facility contracts with diverse main banking players. Other negotiations are in process

- RCGF set a new department aiming at the regional representation of the scheme in bank branches, in counties, regional offices of the Agency for Agricultural Consultancy, Sapard offices. In parallel, new leaflets and guarantee guides were published, the former aiming awareness and visibility, the latter as a complete handbook. RCGF attended to fairs and local professional meetings. Advertising spots were issued on the national TV channel.

- Using the materials collected in those meetings, RCGF increased the guarantee amount and improved its working.
- By Nov. 2003, Deloitte and Touch took over the auditing of the Funds financial statements instead of an internal Audit Committee previously in place. This is very favourable.

2003 data

* Interpretation subject to the variation of the currency exchange rate (depreciation of the Lei by +/- 18%): 1. 1. 2003 : 1€= 34.919 ROL / 31.12.2003 : 1€= 41.117 ROL

* Guarantees granted in 2003 : ROL 1.662.205 Million (564 files) = €40.431.000

This is 118,5% of the annual guarantee ceiling decided as the guideline of the activity.

The average guaranteed amount is €71.690.

Annual serie :

1999	2000	2001	2002	2003
23.911 ROL	144.141	28.766	280.887	1.662.205

Breakdowns :

For medium/long term credits : 32% (216 cases) /// short term credits : 68% (348 files).

Amongst investment guarantees : 121 to the benefit of farmers / 49 trading cics and 46 local councils.

Underlying credits amounted to €20,8 million. The average protection is 63%.

Users : 149 in agricultural sector (20% in value), 21 in food processing industry (40% in value) and 46 in rural infrastructure development (40% in value)

In agriculture, guaranteed credits were used to modernise farm buildings, buy equipment, and purchase assets for vegetal and animal production.

In industry, main uses were new constructions (22%), purchase of assets.

Beneficiaries were in number 159 and in amount % 28% for small businesses (sole proprietors, families, limited Cies) and 95 (72% of the value) for medium ones (Joint Stock Cies) and authorities (local councils)

Worth to note that in the 227 guarantee applications, 139 were in foreign currency (126 in USD and 13 in EUR).

Regarding working capital guarantees, they amounted to €27.217.000 (356 files), including again 73 files in foreign currencies.

They went to agricultural production (39% : seasonal inventories,, liquidity for vegetal and animal goods purchases...) and to food industry (61% : inventories, working capital lines...)

Joint Stock companies took the major part in value (77%) for 85 files.

* Outstanding guarantee amount at 31.12.2003 was ROL 989.225,7 million, i.e. €24.058.800, distributed in 43% for investments and 57% for production.

Number of beneficiaries : 735

Own Funds of RCGF : ROL 465.485 million, i.e. €1.320.986, of which €9 mio as a PHARE allotment. The leverage between outstanding and own funds is 2,13 x. The year was profitable.

Though the a large part of the profit was caused by positive currency adjustments, anyway, the operational result was a profit. A dividend was distributed to shareholders.

Losses :

RCGF pays losses in full at the bank's claim and at the condition that a recovery procedure is initiated.

They are covered by own funds, the interests generated by the Phare allocation and by counterpart funds of the Ministry for a small part. Default risks recorded by RCGF since incorporation is 0,62%.

View on the future

- The outstanding main concern is the recognition by the National Bank of Romania of the inclusion of the Fund's guarantee as a qualified guarantor. This is a paramount question and AECM hopes that it could be solved in a near future as Romania is the only country where no special qualification is given to the guarantee, be it via banking regulation or a specific framework.

-Legal court issues are pending.

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RURAL CREDIT GUARANTEE FUND LITHUANIA

1. Business profile

- State owned company
- Main legal Acts : Resolution 912 of 22.8. 1997 + Resolution 912 of 9 June 2003.
- State support :
 - Fixing of an annual cap of the company's outstanding guarantee commitments : in 2003 : 62,35 Mio €
 - Compensation of losses (budget 2003 offers a max coverage of €551.000)
- Complementary activities to the SME loan guarantee : subsidies to beneficiaries
 - Interest subsidy on the bank loan
 - 80% compensation of the guarantee payment
 - 50% subsidy of the insurance premium for the property mortgaged to the bank
- Number of Staff : 14

2. Facts about 2003 environment

- Better lending environment : increased competition between banks ; lower interest rates
- Uptake of EU Funds (Sapart) stirring the agricultural markets
- Important investments needed in rural areas to increase competitiveness
- International Seminar was held in common with INVEGA
- 1 Lita = €0,29

3. Policies and Fund's strategy in 2003.

- Participation in fairs ; meetings with banks (regional branches) ; increased partnership with business organisations (Chamber of Agriculture ; Business information Centers ; Lithuanian Agricultural Advisory Service, Union of Farmers...)
- New product specification (Government Resolution 912 of June 9th 2003)
 - The fund guarantees the banks up to 70% of the unpaid loan amount (80% for farmers aged less than 40)
 - Eligible sectors :
 - The Agricultural and Food Products Market Regulation Agency (Buffer stock)
 - Farms (sole proprietors, companies, co-operatives)
 - Rural SMEs (services provided to rural population, crafts, rural tourism, forestry, bakers, mills...)
 - Agricultural processing companies
 - Eligible goals :
 - Investments
 - Working capital
 - Conditions :

Investment guarantees	Working capital guarantees
Unrestricted loan duration	Up to 2 years
Max guarantee :	Max guarantee

<ul style="list-style-type: none"> • Farms : €16.000 / • Processing Cies : €261.000 	<ul style="list-style-type: none"> • Farms and SMEs : €87.000 • Processing cics : unrestricted
Guarantee premium : <ul style="list-style-type: none"> • Farms and SMEs : 1,1% • Processing Cics : 5,5% 	Guarantee premium <ul style="list-style-type: none"> • Farms and SMEs : 0,4% • Processing Cics : 2%
Conditions : <ul style="list-style-type: none"> • Self financing : 10% • At least underlying loan asset pledged for the loan 	Condition : <ul style="list-style-type: none"> • Purchased asset or another property pledged in favour of the bank loan.

5. Performance 2003.

(in €000)	2002	2003
Volume of guarantees granted	39.788	52.055
Number of guarantees granted		123
Guarantee outstanding		55.477
Number of beneficiaries		
Responsible own funds		???
Leverage (Outstanding / Own Funds)		

Breakdowns

- Variation percentage of guarantees granted 2003 / 2002 : + 31%
- Long term guarantees granted out of the total : 80% / Short term : 20%
- Average guarantee amount : €185.000
- Partnership with banks : 11 banks, 3 of them being the most significant.
- Jobs created or maintained : 575

6. Results, defaults and losses

The fund net earning in 2003 was positive : €1,3 million, out of which tax and dividends will be paid to the State to the extend of €180.000

Interventions paid in losses in 2003 : €142.390 in 13 files (= 0,26% of the outstanding guarantee portfolio)

In 6 years of activity, losses paid to banks amounted to €2.320.000 ; recovered amounts reached €406.000.

The main causes of failure were :

- Lack of management experience on behalf of entrepreneurs
- Climatic conditions
- Fluctuations in agricultural purchase prices.

The Rural Fund implemented a provisioning policy in classifying risks into 4 categories and attaching fixed provision percentage to each of them : standard (0%) ; sub-standard (20%) ; doubtful (40%) and defaulted / defaulting (100%).

6. Prospects

- In 2004, the public ceiling of protected guarantee outstanding is €63.800.000.
- EU Structural Funds are progressively taking the place of previous instruments (Spart)

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FONDO INTERBANCARIO DI GARANZIA (FIG) : Italy

Mission Statement

The FIG is a special financial vehicle, owned by the Italian State, created in 1961 and specially dedicated to guarantee loans to agricultural enterprises and rural development. In Italy, there is a legal obligation that all credit operations to agricultural undertakings, cooperatives... should be covered either by personal securities or by a recourse to the FIG guarantee.

Legal framework

- Creation : Law 2d June 1961 + Legal Decree 1st September 1993
- Credit to the rural sector : Decree 395 / 1993, art 43.

Operational background

- SMEs belonging to the agricultural sector are the beneficiaries of the guarantee. The guarantee percentage coverage varies from 30 to 70% of the final loss, calculated after assets recovery.
- Ministry of Economy and Finance is the sole shareholder and supervisory authority. It nominates the Board members : 1 representative of the Ministry and 9 representatives of the financial system, elected from banks which contribute by 60% in the payment of the total guarantee premium income (5 delegates), 30% of the premium (3 delegates) and other banks (1 delegate).
The college of revisors is made up of 3 experts from Ministry of Economy, Ministry of Agriculture and Bank of Italy.
- Banks : As users of the system and as members of the Board

Facts about 2003.

- The evolution of the agricultural sector is dominated by the re-definition of the rural areas, the improvement of the production, the focus put on quality environment
- European policies are in the background of the national policies : price policies, harmonization and regulation of the production. Special 2003 concerns were :
 - milk quotas
 - EU enlargement with new orientations in Agricultural policies
 - The doubts about the use of GMO
- By special provisions of Law 268/2003, borrowers who were granted loans at high interest rates in the 90's were allowed to make anticipated reimbursements or to take new, more favourable substitution loans with the original FIG guarantee.
- The Parmalat affair could bear direct or indirect consequences for 5000 rural businesses.
- Basel 2 was another concern for FIG.
- FIG became a associated member of AECEM.

- A new Management Information System platform came into force, improving the communication between FIG and banks.
- New Board members were nominated.

Activity 2003. (Figures in €1000)

In Value, granted guarantees amounted to 1.518.431 concerning 25.963 new credit deals.

Breakdown : 98 million in short term / 630 million in the medium term and €790,5 million in te long term.

The average guaranteed amount per operation is €58.484.

A certain contraction of the Fund's activity can be explained by a number of factors :

- Central and Regional states are limiting their credit subsidies to agriculture (mainly for short term loans)
- Bank globalisation and reorganisation reduce the visibility of the Fund as an instrument to improving credit portfolio quality and to alleviating the capital requirements (FIG's weight is 20% for the risk assets calculation)
- Some administrative burden as well for the granting of the guarantee as for the payment of losses is also mentioned.
- The reduction of guarantees granted for short term credits (98.081.000 against 1,8 billion on average in the 90's) were not compensated by the take-up of long term guarantees (790 million against €400 million in the 90's)

The outstanding amount of guarantees in portfolio was €7.298.274 (composed of 193.194 credits items). The corresponding 2001 and 2002 figures were €7.111 million and 7.316 million.

Regarding the quality of the commitments, the portfolio is divided in 3 parts :

- Standard quality comprises credits "without bad news", for which it is estimated that credit obligations are regularly respected : €6.394.782 (183.828 credits).
- Problem loans for which banks started a recovery procedure against defaulting borrowers : €843.349 (9.095 credits)
- Loans for which the FIG intervention is under examination : €60.143 (271 operations)

Total responsible own funds amounted to €341.796, against 333.346 the year before. The Fund was recapitalized in 1997 by an extraordinary subsidy of €154 million. The year was profitable (accrued net assets of €3.450)

Staff number :

Loss paid to banks amounted to €6,1 million.

Losses refer to years prior to 1999, with a climax for operations granted in 1991, 1992 and 1993. This lag is linked to the practice to pay losses only at the end of the legal action against the defaulted business.

Meanwhile, recoveries amounting to €1,2 million were registered.

Delayed payments compels the Fund to make annual estimates of the risks. The 2003 actuarial study concludes that the probable incurrence of disbursements on the current portfolio amounts to €28,9 million.