Spain Implements Tranched, Adaptive Credit Guarantee Program to Meet Firm Demand

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Original post here.

Spanish companies borrowed nearly €100 billion by the end of August through Spain's tranched credit guarantee program that targeted small and medium-sized enterprises (SMEs), businesses disproportionately impacted by the COVID-19 pandemic. The scheme, announced in mid-March, allowed policymakers to tweak the program's rules as they opened each funding pool.

Under a typical credit guarantee scheme, a sovereign guarantees part or all of a loan to a business, minimizing the lending financial institution's risk and encouraging credit flow. Spain is one of many countries that have instituted such a program since the start of the pandemic.

Spain's credit guarantee scheme split an initially announced €100 billion ($120 billion) in funding into five sections, as shown below, initially backing business financing through banks, then allocating a small portion of the funding through capital markets. In its last funding pool, the Spanish government allocated funds explicitly for the country's tourism sector and firms looking to acquire new vehicles.

To qualify for the guarantees, businesses and freelancers with registered offices in Spain must not be deemed delinquent as of the end of 2019 in Spain's public credit register, the Bank of Spain's Risk Information Center (CIRBE), which details most transactions between financial institutions and their customers. Additionally, the borrowers must not have been in the middle of bankruptcy proceedings as of March 17, 2020.

Banks and other financial institutions eligible to offer these guaranteed loans must be registered and supervised by the Bank of Spain and have a contract with Spain's Instituto de Crédito Oficial (ICO), a state-owned bank. Eligible companies and self-employed individuals can request guaranteed financing through Spain's program at a qualifying financial institution, which will decide to grant the financing based on its own internal procedures. Financial institutions granting guaranteed loans must indicate the government backing for specific loans in their risk management systems and in the CIRBE and must keep financing costs for the borrower in line with costs the financial institution charged prior to the COVID-19 pandemic.

The ICO will pay the financial institution the percentage of the loan the government guaranteed, a unique approach. Every year, the financial entities will pay the ICO between 20 and 100 basis points of the balance of the total amount guaranteed, based on the borrower's firm size and the loan's maturity. The financing firm will also repay the ICO the guaranteed percent of the loan as the borrower makes payments.

Spain appears to be one of few countries that tranched its backing to such a detailed extent over time. As a result, the government was able to make adjustments to its program administration and requirements as it went. For example, in its third round of guarantees, Spain clarified that its backing could not be used to support financing designated for dividend payments and that its funds would not benefit companies headquartered in tax havens.

The guarantee request period for all tranches ends September 30, 2020.

Tranche	Target	Total Allocated	Max Amount	Guarantee	Max Length
1	Loan guarantees: Businesses, including SMEs and the Self-Employed	€20 billion • €10 billion - SMEs and Self-Employed • €10 billion - larger businesses	€1.5 million, with capability to borrow more, subject to EU state aid regulations	• 80% for new loans and 70% for renewed loans for self-employed and SMEs • 60% to larger businesses	5 years
2	Loan guarantees: Businesses, including SMEs and the Self-Employed	€20 billion • €10 billion - SMEs and Self-Employed • €10 billion - larger businesses	€1.5 million, with capability to borrow more, subject to EU state aid regulations	• 80% for new loans and 70% for renewed loans for self-employed and SMEs • 60% to larger businesses	5 years
3	Loan guarantees: Businesses, including SMEs and the Self-Employed	€20 billion • €10 billion - SMEs and Self-Employed • €10 billion - larger businesses	€1.5 million, with capability to borrow more, subject to EU state aid regulations	• 80% for new loans and 70% for renewed loans for self-employed and SMEs • 60% to larger businesses	5 years

	Promissory note guarantees: Businesses	€4 billion	Per company, the amount of the note program the business incorporated prior to April 21, 2020	70%	2 years
	Indirect loan guarantees: SMEs and the Self-Employed	€500 million, allocated to support small business societies throughout Spain that help guarantee loans for smaller businesses			
4	Loan guarantees: Businesses, including SMEs and the Self-Employed	€20 billion • €10 billion - SMEs and Self-Employed • €10 billion - larger businesses	€1.5 million, with capability to borrow more, subject to EU state aid regulations	• 80% for new loans and 70% for renewed loans for self-employed and SMEs • 60% to larger businesses	5 years
5	Loan guarantees: Businesses, including SMEs and the Self-Employed	€12.5 billion • €7.5 billion - SMEs and Self-Employed • €5 billion - larger businesses	€1.5 million, with capability to borrow more, subject to EU state aid regulations	• 80% for new loans and 70% for renewed loans for self-employed and SMEs • 60% to larger businesses	5 years
	Loan guarantees: Tourism sector SMEs	€2.5 billion	€1.5 million	80%	Not announced

and self-employed				
Loan guarantees:				
SMEs and self-employed financing new road transport vehicles	€500 million	Varies, depending on demand	Not announced	Not announced

Tranches 1 and 2 – Bank Lending to Businesses, including SMEs and the Self-Employed

On March 24, the Spanish government opened the first loan guarantee pool of €20 billion targeting self-employed individuals and companies that meet the European Union's definition of an SME: employing fewer than 250 people and having an annual balance sheet less than €43 million.

Though the first tranche targets SMEs and the self-employed, the government earmarked half of the allocated pool of guarantees for companies that do not meet the formal SME requirements.

The Council of Ministers opened the second pool of guarantee funding on April 10, targeting the same swath of companies with identical coverage methodology. Additionally, the government noted in its second announcement that financing costs for loans guaranteed by Spain should generally be lower than other, all else equal loans, given the government's shouldering of risk.

Tranche 3 – Backing Expanded to Capital Markets

The government on May 5 released €24.5 billion of funds. This included €20 billion for loan guarantees, repeating the backing methodology and funding amounts of the first two tranches. It also included €4 billion to guarantee promissory notes that non-financial companies issue through Spain's alternative fixed-income securities market (MARF); and €500 million for Spain's Reinsurance Company (CERSA), which shores up loan backing that the country's Reciprocal Guarantee Societies offer to SMEs. These societies, which are located throughout Spain, assemble business owners and their capital to back member financing through financial institutions.

The government clarified in its third tranche announcement that guaranteed loans cannot be used to make dividend payments and that funds cannot benefit companies headquartered in tax havens.

Tranches 4 and 5 – Tourism and Transportation

On May 19, Spain opened the fourth €20 billion tranche, another SME- and self-employed-targeted pool of loan backing, utilizing the process from the first three sections.

The government released its fifth section of guarantees on June 16, this time aimed at supporting the tourism industry and automotive sector. The final tranche was €15.5 billion. It included €7.5 billion for self-employed individuals and SMEs, €5 billion for large companies, €2.5 billion for the tourism sector, and €500 million for companies and self-employed individuals to acquire vehicles.

Credit Guarantee Usage Figures

As of September 30, 2020, Spanish business owners have used 78% of the €100 billion originally earmarked for credit guarantees.

	Percent of Credit Guarantee Funds Used	Overall Value of New Operations Granted Through Scheme
SMEs and Self-Employed	57% (€57 billion)	€71 billion
Larger Companies	21% (€21 billion)	€31 billion
Total	78% (€78 billion)	€102 billion

New Set of Guarantee Tranches

The Council of Ministers in early July established another tranched credit guarantee program, worth €40 billion, aimed at business investments and productivity growth, specifically those related to process digitization and cleaner energy. Spain's ICO also managed these guarantee lines. On July 28, the government released the first section of such funding. It also allowed businesses to take advantage of the line for non-investment liquidity needs, such as employee pay.

Guarantee Request Period	Total Allocated	Use of Funds	Guarantee Proportion	Max Loan Length
Until December 1, 2020	- €5 billion for self-employed and SMEs - €3 billion for larger companies	- New investments - Worker pay - Supplier payments - Other liquidity needs, such as tax payments	- 80% for SMEs and self-employed - 70% for larger companies	8 years