Assessing Implementation of the Principles for Public Credit Guarantees for SMEs

A Global Survey

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Abstract

This paper presents evidence on implementation of the World Bank Group and Financial Sector Reform and Strengthening Initiative “Principles for Public Credit Guarantee Schemes for Small and Medium Enterprises”. The evidence is based on a self-assessment of 60 schemes in 54 countries. Overall, the results show a fairly decent level of implementation of the Principles, especially in the areas of legal and regulatory framework, mandate and eligibility rules, and claim management process. The results also show several gaps where reform and actions may be warranted, namely identification and accountability of funding sources, corporate governance and risk management, prudential regulatory recognition of guarantees, program/product calibration, and reporting and disclosure.

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Assessing Implementation of the Principles for Public Credit Guarantees for SMEs: A Global Survey

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I. Introduction

Small and medium-sized enterprises (SMEs)¹ are important engines of innovation, growth, job creation and social cohesion in high income and developing economies alike. In high income economies, SMEs undertake the majority of private economic activity, accounting for more than 60 percent of employment and 50 percent of GDP. In emerging economies, SMEs contribute on average to more than 50 percent of employment and 40 percent of GDP (World Bank, 2014). However, SMEs in all countries can only reach their full potential if they obtain the finance necessary to start, sustain and grow their business.

Limited access to finance, particularly bank credit, is a long-standing hurdle for SMEs, with varying severity of financing constraints across countries. In developing countries, between 55 percent and 68 percent of formal SMEs are either unserved or underserved by financial institutions, with a total credit gap estimated in the range of US$0.9 trillion to US$1.1 trillion.² Financing is also a major constraint in advanced economies, where financing gaps for SMEs were exacerbated by the 2008-09 financial and economic crisis. SMEs are typically at a disadvantage with respect to large firms when accessing financing. SMEs face higher transaction costs and higher risk premiums since they are typically more opaque and have less or inadequate collateral to offer. These market failures and imperfections provide the rationale for government intervention in SME credit markets.

An increasingly popular form of government intervention is represented by credit guarantee schemes (CGSs).³ Set up by the government with the purpose of covering some portion of the losses incurred by lenders when SME borrowers default on loans, public CGSs can alleviate the problems faced by SMEs seeking financing thus contributing to their development. However, CGSs can potentially play a more important role, especially in countries with weak institutional environments, by improving the information available on borrowers in coordination with credit registries and bureaus, and by building the credit origination and risk management capacity of participating lenders, for example through technical assistance for the setup of SME units. Moreover, CGSs can also play an important countercyclical role, providing support to small businesses during a downward economic cycle.⁴ However, CGSs may add limited value and prove costly when their design and implementation is flawed.

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¹ SMEs are defined differently across countries and regions, reflecting specificities in the economic, social and regulatory environment. Also, different definitions are adopted for different policy purposes, such as based on profitability for taxation purposes or on number of employees for employment legislation.
³ CGSs are mentioned as one important policy instrument to mobilize bank financing for SMEs by the recently developed G20/OECD High Level Principles on SME Financing (OECD, 2015).
⁴ On the countercyclical role of CGSs during the recent financial crisis see, for example, OECD (2013).
With the objective to develop an internationally-agreed set of good practices that could help governments around the world establish, operate, and evaluate CGSs for SMEs, in 2015 the World Bank Group and the FIRST (Financial Sector Reform and Strengthening) Initiative convened a global task force to identify and draft the “Principles for the design, implementation, and evaluation of public CGSs” (the Principles). The task force included representatives from the Arab Monetary Fund, the Asian Credit Supplementation Institution Confederation, the Association of African Development Finance Institutions, the European Association of Mutual Guarantee Societies, the Ibero-American Guarantee Society, and the Institute of International Finance.

The Principles are a set of good practices that public CGSs either are implementing or intend to implement voluntarily. They cover four key dimensions deemed critical for the success of CGSs: (i) legal and regulatory framework, (ii) corporate governance and risk management, (iii) operational framework, and (iv) monitoring and evaluation. The Principles are drafted at a broad conceptual level to accommodate different legal, regulatory, and institutional settings in various jurisdictions. They are complemented by the Methodology for Assessing Implementation of the Principles, a set of criteria to evaluate application at the country level. The Principles are listed in Annex 1.

This paper represents a first attempt to provide an assessment of the degree of implementation of the Principles across the world based on a self-assessment undertaken by CGSs themselves. Specifically, based on a recent survey of public CGSs this paper provides evidence on where schemes around the globe stand vis-à-vis individual Principles. The survey collects detailed questions on how the key issues related to the Principles are addressed. Assessing a CGS’s implementation of the Principles can be considered a useful tool in measuring the CGS’s adherence to an effective and efficient legal, regulatory, and operational framework. Such an assessment is expected to signal to the authorities any relevant area where reforms and actions may be necessary to improve the effectiveness and efficiency of a CGS. The survey also collects information on the characteristics of public CGSs such as ownership, size, business model, etc. Therefore, this paper also provides up to date evidence on the variety of public CGSs operating across countries.

This paper is related to the extant survey-based literature on CGSs. There are a few global surveys providing both qualitative and quantitative information on CGSs (Doran and Levitsky, 1997; Gudger, 1998; Greene, 2003; Beck et al., 2010) complemented by regional reviews (Saadani et al., 2011 for Arab countries; Samujh et al., 2012, for Asia; Pombo et al., 2013, for Latin America; Vienna Initiative, 2014, for Central and Eastern Europe). However, this paper differs from existing studies in two important aspects: first, it focuses exclusively on public CGSs, i.e. CGSs directly or indirectly controlled by the state; second, it attempts to investigate implementation of the recently introduced Principles.

Overall, we find that surveyed public CGSs show a fairly decent degree of implementation of many individual Principles, with little variation across regions and countries with different levels of economic and financial sector development. In particular, we find that CGSs mostly operate on the basis of a sound legal framework, with a clear separation of responsibilities within the government for exercising ownership on the one hand, and supervision on the other hand. Mandate and eligibility rules are in general well defined as is the claim management process. We also find that a large majority of CGSs systematically analyze their overall performance, including additionality. However, our survey also highlights critical areas where reforms and action is needed. Funding sources are not always identified in the chartering legislation; often, limits on budget appropriations are not set in the relevant legal framework. We also find weaknesses in the corporate governance and risk management framework, especially in the board appointment process and the use of appropriate techniques to identify and manage credit risk. In many jurisdictions the guarantee issues by the CGS does not provide regulatory capital relief to partner lenders and is not recognized for loan classification purposes. A few CGSs use the guarantee coverage ratio as an operational tool to differentiate their offering. Finally, some CGSs do not publish financial statements and do not disclose non-financial information.

The remainder of this paper is organized as follows. The next section presents the sample and methodology used in this paper and discusses the characteristics of public CGSs around the world. Section III is the core of the paper: it presents the results of the survey for each of the four key topics addressed by the Principles: (i) legal and regulatory framework, (ii) corporate governance and risk management, (iii) operational framework, and (iv) monitoring and evaluation. Section IV concludes, summarizing the main areas for improvement and pointing to potential developments in the knowledge agenda on public CGSs.

II. The sample and some general characteristics

In line with the scope of application of the Principles, for the purpose of this survey a public CGS is defined as an institution whose mandate encompasses the provision of credit guarantees to financial institutions to mobilize financing to SMEs in which the state retains de jure or de facto control.6

The survey is based on a questionnaire, drawn from the Methodology for Assessing Implementation of the Principles, which was submitted to the members of the regional associations and networks of public CGSs in Africa, Asia, Europe, Latin America and Middle East and North Africa (MENA), and bilaterally to other CGSs which are not part of any association/network.7 A total of 62 responses were received; however, two did not meet the

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6 CGSs can be established, funded and operated by entities other than the state. According to the nature of the CGS operator, it is possible to identify three additional types of CGSs: mutual guarantee associations, international schemes and corporate CGSs. However, this paper only focuses on public CGSs.

7 The full survey is available in Annex 3.
survey’s definition of CGS and were therefore excluded. The remaining responses constituted the basis for this paper.\footnote{A few CGSs did not respond to each and every question. Nonetheless, the overall individual response rate is excellent.}

Our sample includes 60 CGSs across 54 countries, both developing and advanced economies. Specifically, we have information on CGSs in 22 high-income, 29 middle-income and 3 low-income countries. In terms of regional distribution, we have information on four CGSs in Africa; 13 located in Asia; 15 in Europe; 11 based in MENA; and 17 in the Western Hemisphere.\footnote{For the purpose of this paper, the Western Hemisphere includes countries located in North America, Latin America and the Caribbean.} We have, therefore, a very well balanced sample by both income level and regional grouping. Annex 2 provides a full list of countries and CGSs included in the survey.

One important caveat with regards to the data in the survey is in order. The data come directly from responses provided by officials of CGSs that participated in the surveys. The data were not verified by a third-party. However, CGSs’ senior managers had an opportunity to validate their institutions’ data. Moreover, we cleaned and double-checked the survey responses for consistency, including vis-à-vis annual reports and other publicly available information. For all these reasons, the information provided cannot be interpreted as a full diagnostic of participating schemes. The latter requires a review of the legal environment and financial sector in which the CGS operates supplemented by qualitative and judgmental analysis to qualify and contextualize the data.

CGSs are an important tool used by governments to promote access to finance for SMEs in practically all countries around the world. In many countries, CGSs have existed since the beginning of the 20th century (Beck et al., 2010), but they have experienced unprecedented growth over the last two decades. In particular, CGSs have been an instrument of choice for policy makers to improve access to finance by SMEs during the recent global financial and economic crisis. These general patterns are reflected in our sample (Table 1). The median age for all CGSs is 21 years, with little variation across different income groups and regions. The only exception is MENA, which is home to the younger CGSs, with a median age of 12 years. However, it is interesting to note that more than a quarter of public CGSs in our sample were established after 2007, when the global financial crisis started off.

Typically, public CGSs are institutions owned, managed and controlled by the government, which provides strategic direction and appoints board members and senior management. The extent and form of government ownership of CGSs, however, can vary (Figure 2). While 78 percent of the CGSs surveyed are entirely owned and controlled, directly or indirectly, by the national, regional or local government (including through state-owned development finance institutions), in another 13 percent the private sector participates as minority shareholder, holding between 2 percent and 41 percent of total shares. Typically, private sector minority shareholders include both commercial financial institutions and SMEs. In this type of CGS, the government retains control of the institution, while the private sector owns part of its capital.
Interestingly, in 8 percent of the CGSs surveyed the government owns less than 50 percent of the capital, while providing policy and strategic direction to the CGS, ensuring that the latter retains its focus on developmental activities. The mixed ownership model is very popular in the MENA region, where 55 percent of the surveyed CGSs have private sector participation in the CGS’ capital, mostly by partner financial institutions.

Table 1
General characteristics, median values: 2014

<table>
<thead>
<tr>
<th>Region</th>
<th>CGSs</th>
<th>Age*</th>
<th>Outstanding guarantees (US$ mn)</th>
<th>Outstanding guarantees (% GDP)</th>
<th>Employees</th>
</tr>
</thead>
<tbody>
<tr>
<td>All CGSs</td>
<td>60</td>
<td>21</td>
<td>203</td>
<td>0.11</td>
<td>99</td>
</tr>
<tr>
<td>Income group</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>High Income</td>
<td>23</td>
<td>21</td>
<td>727</td>
<td>0.33</td>
<td>189</td>
</tr>
<tr>
<td>Upper Middle Income</td>
<td>24</td>
<td>19</td>
<td>178</td>
<td>0.07</td>
<td>32</td>
</tr>
<tr>
<td>Lower Middle Income</td>
<td>13</td>
<td>24</td>
<td>32</td>
<td>0.10</td>
<td>36</td>
</tr>
<tr>
<td>Low Income</td>
<td>17</td>
<td>19</td>
<td>220</td>
<td>0.05</td>
<td>64</td>
</tr>
</tbody>
</table>

* As of 2016.

In terms of size, measured by the total outstanding guarantees in 2014, CGSs in high-income countries are four times as large as those in upper-middle income countries, which in turn are 5.5 times as large as CGSs in lower-middle and low income economies (Table 1). If outstanding guarantees are scaled by GDP, however, the gap between developed economies and developing countries narrows down, with a median of 0.33 percent for high-income countries compared to 0.10 percent for developing economies. The region with the largest schemes is Europe, where the median size is 0.29 percent, in line with the median for high-income countries. However, behind these seemingly low median values there is large cross-CGS variation, ranging from very small and relatively young CGSs such as in Canada or Iraq to well established CGSs such as the Japanese or the Korean schemes, whose outstanding guarantees in 2014 amounted to 5.7 and 3.3 percent of GDP, respectively. In terms of number of employees, CGSs in high-income countries are much bigger than those located in developing countries. This result is largely driven by the Asian (non-developing countries) schemes, which show a median size of 371 employees.

CGSs are set up with the purpose of providing third-party credit risk mitigation to lenders to stimulate debt financing to SMEs. CGSs can guarantee loans directly or in the form of counter-guarantees granted to other public and/or private schemes. In our sample, all but one CGSs offer direct guarantees to lenders. In four cases, these are offered along counter-guarantees to other CGSs, while only one CGS (Japan) offers exclusively counter-guarantees. Within their mandate, CGSs in general offers several programs and products. The median CGS in our sample provides 4 programs/products. The number of programs/products seems to be associated with the age and track record of a CGS: the older the CGS, the larger is its offering. Asian (MENA) CGS, with the older (younger) median age, are those more (less) sophisticated in terms of program/product development.
Public CGSs can offer additional services to both lenders and borrowers to address issues other than those related to collateral that might be hindering access to credit by SMEs such as lack of capacity. In fact, a large majority of CGSs offer ancillary services, primarily advisory and training services to SMEs. More than half of surveyed CGSs provide SMEs, either directly or indirectly, with technical assistance and capacity building. This finding is broadly consistent across income and regional groups. On the other hand, about one third of surveyed CGSs offer assistance to their client financial institutions, though this is mostly found in developing economies, confirming the potentially important role CGSs can play in countries with weak institutional environments. Forty-six percent and sixty-two percent of CGSs in low and lower-middle income economies, respectively, provide advisory and training services to financial institutions.

Although beyond the scope of the survey, the questionnaire included a few general questions related to the performance of the CGSs. In particular, CGSs were asked to report on the number of SMEs served, their number of employees, capitalization levels and the nonperforming rate of their portfolios in 2014. This allows for the observation of some cross-sectional performance trends (Table 2). The median CGS served 1,383 SMEs in 2014 (flow), corresponding to a median outreach of 1.6 percent of the total estimated universe of SMEs by country.\(^\text{10}\) Outreach is an important dimension of the CGS’s overall performance as it measures the ability of the CGS to meet demand for guarantees. Outreach outcomes vary significantly by country: for example, CGSs in Mexico and Japan guaranteed loans to more than 130,000 SMEs in 2014, while in the same year schemes in Bosnia & Herzegovina and Jamaica (and others) served fewer than 30. Overall, it appears that older and well established CGSs display higher outreach outcomes.

<table>
<thead>
<tr>
<th>Table 2</th>
</tr>
</thead>
<tbody>
<tr>
<td>Performance, median values: 2014</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>All CGSs</th>
<th>1,383</th>
<th>1.6</th>
<th>29</th>
<th>3.3</th>
<th>2.5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income group</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>High Income</td>
<td>6,507</td>
<td>2.0</td>
<td>30</td>
<td>4.1</td>
<td>2.9</td>
</tr>
<tr>
<td>Upper Middle Income</td>
<td>1,139</td>
<td>0.9</td>
<td>29</td>
<td>2.9</td>
<td>3.0</td>
</tr>
<tr>
<td>Lower Middle Income and Low Income</td>
<td>887</td>
<td>1.6</td>
<td>21</td>
<td>1.0</td>
<td>1.0</td>
</tr>
<tr>
<td>Region</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Africa</td>
<td>77</td>
<td>0.3</td>
<td>8</td>
<td>1.7</td>
<td>17.1</td>
</tr>
<tr>
<td>Asia</td>
<td>17,293</td>
<td>2.7</td>
<td>33</td>
<td>3.2</td>
<td>1.2</td>
</tr>
<tr>
<td>Europe</td>
<td>1,139</td>
<td>0.9</td>
<td>17</td>
<td>3.8</td>
<td>2.9</td>
</tr>
<tr>
<td>MENA</td>
<td>829</td>
<td>2.2</td>
<td>22</td>
<td>4.4</td>
<td>3.8</td>
</tr>
<tr>
<td>Western Hemisphere</td>
<td>6,531</td>
<td>3.4</td>
<td>164</td>
<td>3.0</td>
<td>2.0</td>
</tr>
</tbody>
</table>

* Number of SMEs served divided by total SMEs in the country.
** Number of guarantees issued divided by number of employees.
*** Outstanding guarantees divided by total capital.
**** Nonperforming guarantees divided by outstanding guarantees.

Financial sustainability is another important aspect of the CGS’ performance. Although CGSs are not profit maximizing entities, they should still be able to maintain an adequate capital base relative to their liabilities on a going concern basis. Financial sustainability indicates the degree of reliance of a CGS on public financial support. A first indicator of financial sustainability that we are able to calculate is a measure of productivity, i.e. the ratio of number of guarantees to number of employees. The median level for our sample is 29. However, this figure masks important regional differences. Equally, important it conceals differences in the business model of CGSs, especially in terms of delivery approach. In general, CGSs provide guarantees on the basis of two methods or both: the individual approach and the portfolio approach. Under the former, guarantees are provided on a loan-by-loan basis; under the latter, lenders attach guarantees to SME loans within pre-agreed eligible categories and without consultation with the CGS. By design, efficiency levels are expected to be lower under the individual approach than under the portfolio method. As a matter of fact, in our sample CGSs which employ the individual approach for the majority of their guarantees display a productivity ratio of 22 compared to 80 for CGSs which apply a portfolio approach. The most efficient CGSs in our sample are those based in the Western Hemisphere, particularly in Latin America, regardless of the delivery method adopted.

Another measure of financial sustainability is the capitalization of the CGS, typically proxied by the leverage ratio, i.e. the ratio of outstanding guarantees to capital. The median CGS in our sample shows a leverage ratio of 3.3 times in 2014. CGSs domiciled in high-income economies exhibit higher leverage ratios (4.1 times) than those in upper-middle income (2.9 times) and lower-upper and low income economies (1 to 1). In terms of regional grouping, we find that the leverage ratio ranges from 1.7 times in Africa (the lowest) to 4.4 times in MENA (the highest). The median rate of nonperforming guaranteed loans, an indicator of asset quality of CGSs, is 2.5 percent. This ranges from a median 1.2 percent in Asia to 17.1 percent in Africa.

These basic characteristics provide a first glance at differences in the way public CGSs operate across countries. The next sections will discuss in detail the level of implementation of the Principles along the following key areas which are critical to the success of a CGS: (i) legal and regulatory framework; (ii) corporate governance and risk management; (iii) operational framework, and (iv) monitoring and evaluation.

III. Assessment of implementation of the Principles

III.A. Legal and regulatory framework

Principles in this area are intended to provide the foundations of an effective and efficient CGS. They provide the legal basis and the regulatory and supervisory framework.

Under Principle 1, a CGS should operate on the basis of a sound and clearly defined legal framework. This is essential for communicating key expectations to shareholders, boards, management, and all other stakeholders, including SME borrowers and the general public. The underlying aim of a strong legal framework is to make the broad policy directions of the government and the “rules of the game” clear for everyone, enhancing the credibility and
reputation of the scheme. From this perspective, a large majority of the surveyed CGSs (87 percent) are established by law, decree or other special legislation. Exceptions to this rule are equally found across countries in different regions and with different levels of economic and financial sector development. Of the surveyed CGSs, 80 percent are established as an independent legal entity (Figure 1).

The legal framework should also clarify the ownership policy of the government, or general terms and conditions, which apply to the government’s investment, and the manner in which the government will exercise its ownership, including who is responsible and accountable for representing the shareholder (Ministry, agency etc.). More than three-quarters of surveyed CGSs reported that their chartering legislation does indicate the ownership entity. The Ministry of Finance is the most common form of ownership entity, with 31 percent of responses, followed by the Ministry of Economy with 18 percent. Other less common ownership entities include the central bank, various government agencies and development finance institutions. There is no significant variation by income group or region.

**Figure 1**

Legal form, number

![Chart showing legal form, number](chart.png)

In developing the Principles, the task force recognized that governments may choose to operate a CGS through development finance institutions as long as the CGS has financial, managerial and operational independence from the primary legal entity. However, pay-as-you-go schemes funded by annual budgetary subventions and CGSs operated by government agencies should be discouraged because of the lack of transparency and reliability of such arrangements. In this respect, nine CGSs in our sample are indeed operated through a state-owned development finance institution, while three are run by a government agency or ministerial department (Figure 1). Of these 12 CGSs, nine have financial independence such as a separate capital and budget; ten have managerial autonomy such as distinct governing body, management and/or staff; and only six have an operational framework different from that of the primary entity. The arrangement where the CGS is operated as a program of a third-party entity is mostly found in the Western Hemisphere, with 8 cases.
It is essential that sufficient capital and government support be available to ensure an effective implementation of the CGS and its subsequent viability. The tendency to set up small CGSs in some instances in the past seriously undermined the confidence of partner lending institutions. The various forms that state funding may take include: (i) direct financial support through budget provisions or subsidies; and (ii) indirect financial support, including preferential access to finance, debt financing, equity financing, tax treatment and less rigorous financial accounting standards. Principle 2 indicates that the sources of the CGS, including reliance on subsidies, should be transparent and publicly disclosed. In our sample, the chartering legislation indicates the sources of funding for about three-quarters of CGSs. The most common form of government funding is represented by direct subsidies, accounting for 38 percent of all sources of funding, followed by equity endowments (28 percent) and government guarantees (16 percent). Interestingly, direct subsidies are the most important funding source for high-income countries, mostly in Europe, representing half of all funding (Figure 2).

Figure 2
Ownership, frequencies (%)

Funding, frequencies (%)

To prudently manage its capital structure, the CGS should not borrow from public or private debt markets, and the relevant legal (or regulatory) framework should indicate the maximum leverage the CGS would comply with. Yet maximum leverage ratios are set in only two-thirds of the surveyed CGSs; interestingly, half of CGSs in high-income economies do not specify minimum capital adequacy standards. The median maximum permissible leverage ratio is 8 times across our sample, with little variation by income group and region.

Another important characteristic of the CGS’s funding arrangements, distilled in Principle 2, is that to contain fiscal risk for the government the chartering legislation should set limits to subsidies and other forms of budget appropriations. Moreover, funding arrangements should be periodically reviewed and audited by the supreme audit institution or other relevant body. For more than half of surveyed CGSs which declared to receive subsidies there are no limits on budget appropriations referenced or described in the relevant legislation, and this is the especially the case in MENA. On the other hand, in more than three-quarters of CGSs in our
sample funding use and limits are systematically reviewed by the supreme audit institution or equivalent mandated body, a finding common across income and regional groupings.

A desirable feature of a CGS is to share ownership with private entities, and our results show that this is actually the case in 22 percent of CGSs in our sample. Mixed ownership presents several advantages: it provides an additional source of funding to the CGS; it contributes to advance knowledge of the target market; it exposes the CGS to good corporate governance practices; and it introduces peer pressure, shared responsibility and transparency in the decision-making process, hence reducing moral hazard on the part of both lenders and SME borrowers. Principle 3 explicitly states that the legal framework establishing the CGSs should encourage (but not force) private sector participation in the ownership structure of the CGS. Such a provision is codified in only 26 percent of the surveyed CGSs.

When part of a CGS’s capital is held privately, special problems can arise. Governments can behave in ways that work against the interests of minority shareholders. In this case, it is important to recognize the rights of all shareholders and promote equitable treatment. This would benefit the government as well as the minority shareholders, since the government’s reputation as owner affects (positively or negatively) both the CGS’ ability to attract private funding and its valuation. Moreover, by functioning as a check on costly or unreasonable demands from the ownership entity or another part of the government, equitable treatment of shareholders can also improve the CGS’ performance. Ensuring equitable treatment of minority shareholders by promoting their participation in the CGS’ governance should be explicitly recognized in the legal framework, according to Principle 3. We find that private sector shareholders have the right to actively participate in the CGS’s decision-making through board representation in all the surveyed CGSs which have minority shareholders.

Credit guarantees must be safe and liquid securities which can be enforced juridically if they are to be used by commercial lenders. Therefore, a certain degree of regulation and supervision is necessary. It is an accepted principle of state ownership in general that there should be a clear separation of responsibilities within the government for exercising ownership, on the one hand, and for exercising regulatory and supervisory responsibilities, on the other hand.\textsuperscript{11} This is important to prevent conflict of interests and avoid undermining both government functions. To exploit economies of scale and reduce overall cost of independent oversight, supervisory powers should be vested in one entity, preferably the financial sector supervisor. Supervisory accountabilities are clearly defined in the chartering legislation in 83 percent of CGSs in our sample, where the body in charge of oversight is explicitly indicated. Regardless, all but four of the CGSs in our sample are actually supervised. The most common supervisory body is the financial sector regulator (Figure 3), accounting for one third of all responses, followed by the Ministry of Finance (20 percent). The financial sector regulator is found to be the supervisor of choice in lower-middle and low income countries (47 percent of all responses), especially in Africa (75 percent). Interestingly, 19 of the CGSs in our sample declared that they are supervised by more than one public oversight body.

\textsuperscript{11} See World Bank, 2014; and OECD, 2005.
As Principle 4 asserts, supervision should be calibrated on the basis of the nature and risks of the product and services offered by the CGS. This means in practice that the supervisor should (i) ensure that the CGS performs only those activities explicitly mandated by its chartering legislation; (ii) determine that the CGS has adequate corporate governance arrangement in place; (iii) determine that the CGS satisfies minimum capital adequacy requirements and takes remedial measures should this not happen; and (iv) determine that the CGS has adequate risk management strategies and policies and procedures in place, and procedures for the identification, classification, provisioning and management of problem assets. We find that all the areas listed above are equally within the scope of supervision of CGSs across income and regional groups. Moreover, the supervisor has the legal authority to enforce conduct and prudential standards when necessary for 86 percent of respondents. In MENA, however, five of the eleven respondents reported that the supervisor does not have such enforcement powers.

**Figure 3**
Supervision of CGSs, frequencies (%)

III.B. Corporate governance and risk management

Corporate governance and risk management, topics of the second group of the Principles, are critical building blocks for an effective and efficient CGS. They ensure that the CGS designs and executes strategies in line with its mandate and policy objectives. Sound corporate governance and risk management also ensure proper monitoring of both financial and non-financial risks.

Principle 5 states that a public CGS should have a clearly defined mandate, spelled out in the chartering legislation. Clearly stating the mandate of the CGS is necessary for defining accountability, determining the scope of its activities, and forming the basis for more specific targets for its operations. Ideally, the mandate should be set in the relevant legislation which creates the CGS. Mandates are expected to include at least the following two components: (i) the target SME market, and (ii) the main business lines of the CGS. All but ten of the surveyed CGSs
have a clearly defined mandate, encompassing either the target SMEs or the lines of business of the CGS. Only in half of the CGSs in our sample, both target market and business lines are indicated in the mandate.

Over time, CGSs can come to engage in activities and pursue objectives that were never envisioned by the government. In other cases, the evolution of the financial system, client needs and shifting public policy objectives, may render the mandate no longer relevant or appropriate. Therefore, periodic mandate reviews through an explicit and transparent mechanism stated in the legal framework are in order to assess the continuing validity of the CGS’ mandate. However, of those CGS whose chartering legislation prescribes a mandate, only two-thirds have an explicit mechanism for periodically reviewing its relevance. These CGSs constitute the majority in Europe.

In accordance with its mandate, the CGS should develop coherent strategies and specific programs for different target sectors and groups. Acknowledging that different SME target sectors and groups may require different operational support, the CGS should develop tailored strategies, including one for effective communication. This is actually the case for the vast majority of the CGSs in our sample (all but four).

Political intervention is one of the major threats for an effective and efficient CGS. This is typically a consequence of a lack of independence of the board of directors and senior management of the CGS. Political intervention can be limited by ensuring a transparent and structured process for the appointment of independent and qualified board members. This is the gist of Principle 6. We find some gaps in this area, especially in developing economies. Twenty percent of surveyed CGSs do not have a clear board appointment process spelled out in the legal framework, charter or other constitutive document. Of those CGSs which have such a process, one-third do not have minimum qualification criteria to ensure the professionalism of board directors. These are CGSs mostly located in developing countries. In 17 percent of the surveyed CGS with a board appointment process in place, there are no board term limits. Again, these are only found in developing countries. Finally, in 35 percent of CGSs in developing economies, there are no independent and unaffiliated board directors from the private sector.

A CGS should have a robust internal control framework in place. The systems, standards, and procedures that form a CGS’ control environment safeguard the integrity and efficiency of its governance and operations. Effective internal controls allow top managers to know what is happening in the organization and whether their instructions are being carried out. Overseeing and enforcing a system of internal controls should be an independent and empowered internal audit and compliance function. Such a function should place particular emphasis on monitoring the control systems and evaluating risk exposures related to the CGS’ governance, operations and information systems. Moreover, the internal audit and compliance function should be endowed with adequate resources and the power to conduct investigations at the request of the board. In our sample, only six CGSs, found equally across income groups and regions, do not have an internal audit and compliance function. For those which have one, only in two cases do the internal auditors not have investigative powers.
The ability of CGSs to identify, measure, monitor and control the risks they face as well as to determine that they hold adequate capital against those risks is a critical component of the overall corporate governance framework and ultimately an essential determinant of performance. According to Principle 8, any public CGS should adopt a sound enterprise risk management framework as part of the internal control environment. The enterprise risk management framework should be approved by the board and subject to periodic reviews to assess its continuing relevance. Yet 13 percent of the surveyed CGSs responded that they do not have an enterprise risk management framework in place. These CGSs are found in countries with different levels of economic and financial development. For those CGSs which declared to adopt an enterprise risk management, the latter is approved by the board and reviewed periodically in 96 percent of them.

Credit risk is the main risk faced by CGSs. The measurement and management of credit risk should rely on appropriate quantitative and qualitative techniques. Overall, 83 percent of all CGSs in our sample have in place a credit risk management framework supported by an appropriate analytical toolkit (Table 3). Those CGSs which do not rely on relevant credit risk infrastructure are found primarily in developing economies, particularly in the Western Hemisphere. An effective credit risk management should also establish and enforce a set of relevant exposure limits to mitigate concentration risk. Almost three-quarters of CGSs in our sample systematically adopt exposure limits to manage credit risk. Credit exposures are mainly managed through ceilings to specific industries, which account for 34 percent of all risk limits, followed by financial institutions exposure limits and geographical ceilings (both 20 percent). Other common exposure limits include loan size and capital allocated to a certain program/product.

<table>
<thead>
<tr>
<th>Table 3</th>
<th>Enterprise risk management, frequencies (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Income</td>
</tr>
<tr>
<td></td>
<td>All</td>
</tr>
<tr>
<td>Credit risk management</td>
<td>83</td>
</tr>
<tr>
<td>Liquidity and market risk management</td>
<td>70</td>
</tr>
<tr>
<td>Operational risk management</td>
<td>81</td>
</tr>
</tbody>
</table>

CGSs can reduce their own exposures to loan defaults through a number of techniques such as counter-guarantees, co-guarantees, loan sales or portfolio securitization, depending on the level of development and sophistication of local capital markets and financial products. We find that only 47 percent of CGSs in our sample use risk management tools to manage their overall exposures. About one-third of surveyed CGSs reinsure their portfolios with a counter-guarantor. This is especially the case in Europe and in the Western Hemisphere, where counter-guarantees are generally provided by regional, multilateral institutions. Another 14 percent of surveyed CGSs uses co-guarantees to mitigate credit risk.

An effective risk management framework should also encompass guarantee evaluation policies and practices. This is the case in 90 percent of the CGSs in our sample. Finally, the credit
risk management framework should include tools to identify environmental, social, and corporate governance risks associated with the CGS’ guarantee business to encourage sustainable and socially responsible business development by both SMEs and lenders. Yet, only 58 percent of surveyed CGSs have implemented this component of Principle 8. The most “socially responsible” CGSs are found in Asia.

A second type of risk a CGS confronts is liquidity and market risk. A public CGS should develop an effective liquidity and market risk management framework to ensure that it meets claims and hedges against adverse movements in market prices. Reliable governance arrangements, management information systems, analysis of liquidity requirements, and contingency planning (for example, a concessional standby line of credit from the government) are crucial elements of a strong liquidity and market risk management system. In this respect, 70 percent of all CGSs in our sample have a liquidity and market risk management framework in place, with relatively limited differentiation across income levels and regions (Table 3). Analysis of liquidity requirement is the most common tool used to manage liquidity risk, adopted by 43 percent of all CGSs. The CGS should also have a transparent investment policy that establishes an investment framework consistent with the mandate and strategic objectives of the CGS, the approved risk profile, and monitoring procedures. Although there is no one-size-fits-all approach, the investment policy should be guided by appropriate portfolio management criteria. Seventy-seven percent of surveyed CGSs responded positively to the question of whether they are guided by an investment policy when they place their liquidity.

A final type of risk faced by CGSs is operational risk, or the risk of a loss stemming either from failures in the CGS’ systems and procedures or from events outside the control of the organization. To assess and control operational risks, the CGS should establish and document a relevant operational risk management framework. Codes of conduct and recruitment policies are important to minimize unethical behavior within the organization. On the other hand, business resumption planning should be an important component of the operational risk framework to ensure continuity of operations in the event of a technology breakdown or natural disaster. From this perspective, it emerges that 48 CGSs in our sample have an operational risk management framework in place (Table 3). About half of these CGSs implement codes of conduct rules, recruitment policies and business resumption plans to mitigate operational risks.

III.C. Operational framework

A clear operational framework, the subject of the third area covered by the Principles, provides CGSs with a course of action comprising essential working parameters.

CGSs are generally aimed at widening access to finance for a target group of unserved or underserved SMEs. While definitions of SMEs may vary within the country, it is important that the target groups are clearly determined in the policies or other relevant operational framework of the CGS. It is also desirable that eligibility criteria are made publicly available and periodically reviewed. Typical eligibility criteria for SMEs include size, sector and the age of firms. All but one surveyed CGSs reported having eligibility rules for their target SME markets, while 90 percent of all CGSs communicate those rules to the general public. Seventy-three percent of CGSs in our
sample periodically assess the relevance of their eligibility criteria for SMEs. These findings are broadly consistent across countries in different regions and with different levels of economic development.

Another desirable feature of the modus operandi of a CGS, included in Principle 8, is to determine and communicate qualification criteria for lenders. Not every lender in the country has strategic interest and ability to reach out to SMEs; equally important, not every lender has a sound financial profile to effectively partner with the CGS. Therefore, the CGS should introduce minimum requirements for lenders to participate in the scheme. Yet only two-thirds of surveyed schemes which answered this question declared that they have adopted qualification criteria for partner financial institutions.

A CGS should also clarify the credit instruments targeted. These can be summarized in two broad areas: working capital and investment finance. The former is typically used to finance day to day operations of company, and has a short maturity; the latter is used to finance the purchase of productive assets and has longer tenures. Whereas working capital finance may be important for sustaining jobs in firms which could become insolvent due to insufficient short-term credit, investment finance is essential for long-term job creation and economic growth. Eighty-five percent of CGS in our sample offers coverage for both credit instruments, in almost equal proportion. The remaining 15 percent provides credit guarantees only for one instrument, typically for investment finance. Regardless of the type of credit instrument targeted, the guarantee issued by the CGS should cover the principal amount of the loan and to a limited extent the unpaid interest. From this perspective, while all surveyed CGSs reported that they guarantee the principal, only 41 percent provide coverage for part of the unpaid interest as well.

A fundamental dimension of the business model of any CGS concerns the modalities of extension of guarantees to lenders. As discussed in Section II, there are two generally adopted methods: the individual approach and the portfolio approach. The choice of the delivery method should involve an analysis of the trade-offs among the key outcomes of the CGS: outreach, additionality and financial sustainability. Ideally, the CGS should combine both approaches, taking into account the specific contours of the programs/products it intends to develop, as well as the degree of development and sophistication of both the financial sector and partner financial institutions.

We find that 49 percent of the CGSs in our sample use only the individual approach, while 10 percent use only the portfolio approach (Table 4). Forty-one percent use a combination of the two approaches. Interestingly, the portfolio approach is used more in developing economies than in high-income countries (14 percent vs. 9 percent), and even when a mixed approach is used the volume of guarantees delivered through the portfolio method outnumber those provided on a loan-by-loan basis. The region where the portfolio approach is more widely used is the Western Hemisphere, where about one-third of all CGSs use exclusively the portfolio method compared to 18 percent adopting solely the individual approach. We also find that the individual approach is the ordinary/default option for 69 percent of all surveyed CGSs, whereas the portfolio approach is the elected choice for 17 percent of CGSs. The contrast with actual usage of delivery
methods is explained by the fact that delivery methods are flexibly used to target different client groups. For example, the portfolio approach is used by 15 percent of all CGSs for relatively small loans, and by 12 percent for special target groups. On the other hand, the individual approach is used to target SMEs requiring relatively large loans by 22 percent of CGSs.

In order to avoid the danger of moral hazard, it is essential that the CGS distributes the credit risk of SMEs among all the three actors involved in the scheme, i.e. SMEs, lenders and the CGS itself, so as to maximize incentives to keep default and claim rates as low as possible. CGSs can distribute risk to the lender by means of the guarantee coverage, usually expressed as a percentage. The guarantee coverage should be high enough to induce lenders to participate in the scheme. However, it should not eliminate the risk for lenders entirely. The guarantee coverage ratio should be clearly indicated in the legal agreements between the CGS and the lenders. This is actually the case for all but one surveyed CGS. Moreover, 61 percent of CGSs share losses pari passu with the partner lenders, whereas 21 percent offer first-loss cover. The remaining 18 percent use a mix of both approaches.

Table 4
Operational parameters, median values (%)

<table>
<thead>
<tr>
<th>Delivery method</th>
<th>Income</th>
<th>Region</th>
<th>All</th>
<th>High</th>
<th>Middle</th>
<th>Low</th>
<th>Africa</th>
<th>Asia</th>
<th>Europe</th>
<th>MENA</th>
<th>Western Hemisphere</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individual</td>
<td>49</td>
<td>70</td>
<td>46</td>
<td>38</td>
<td>33</td>
<td>50</td>
<td>47</td>
<td>55</td>
<td>18</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Portfolio</td>
<td>10</td>
<td>9</td>
<td>17</td>
<td>8</td>
<td>0</td>
<td>7</td>
<td>0</td>
<td>0</td>
<td>29</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Both</td>
<td>41</td>
<td>22</td>
<td>38</td>
<td>54</td>
<td>67</td>
<td>43</td>
<td>53</td>
<td>45</td>
<td>53</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Guarantee coverage ratio</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average</td>
<td>70</td>
<td>75</td>
<td>65</td>
<td>66</td>
<td>80</td>
<td>73</td>
<td>73</td>
<td>69</td>
<td>50</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Min</td>
<td>50</td>
<td>50</td>
<td>50</td>
<td>50</td>
<td>70</td>
<td>50</td>
<td>50</td>
<td>58</td>
<td>20</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Max</td>
<td>80</td>
<td>80</td>
<td>80</td>
<td>80</td>
<td>85</td>
<td>88</td>
<td>80</td>
<td>80</td>
<td>80</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Capital relief</td>
<td>Yes</td>
<td>70</td>
<td>74</td>
<td>62</td>
<td>75</td>
<td>67</td>
<td>62</td>
<td>73</td>
<td>64</td>
<td>76</td>
<td></td>
</tr>
<tr>
<td>No</td>
<td>20</td>
<td>17</td>
<td>25</td>
<td>17</td>
<td>33</td>
<td>15</td>
<td>14</td>
<td>27</td>
<td>24</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Don’t know</td>
<td>10</td>
<td>9</td>
<td>13</td>
<td>8</td>
<td>-</td>
<td>23</td>
<td>13</td>
<td>9</td>
<td>-</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pricing</td>
<td>Average</td>
<td>2.4</td>
<td>2.0</td>
<td>2.5</td>
<td>2.0</td>
<td>2.4</td>
<td>1.6</td>
<td>2.3</td>
<td>2.3</td>
<td>3.0</td>
<td></td>
</tr>
<tr>
<td>Min</td>
<td>1.0</td>
<td>1.5</td>
<td>1.0</td>
<td>1.5</td>
<td>1.0</td>
<td>1.5</td>
<td>0.7</td>
<td>1.0</td>
<td>1.0</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Max</td>
<td>2.3</td>
<td>2.0</td>
<td>2.7</td>
<td>2.5</td>
<td>1.0</td>
<td>3.0</td>
<td>2.5</td>
<td>2.0</td>
<td>3.0</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The typical guarantee coverage ratio applied by the median CGS in our sample is 70 percent, with a minimum of 50 percent and a maximum of 80 percent (Table 4). Therefore, we find no evidence of guarantee coverage ratios of 100 percent, which would defeat the important principle of risk sharing. On the contrary, we find that some CGSs in Latin America offer guarantees of as low as 20 percent. According to Principle 11, the guarantee coverage ratio should correlate with the SME target groups the CGS intends to serve. Yet only 63 percent of the CGSs in our sample set specific coverage ratios for different programs/products. In this respect, we observe some variation by region: while African CGSs do not change the guarantee coverage on the basis of the programs offered, 81 percent of CGSs in the Western Hemisphere use this important operational parameter as a tool to differentiate their offerings. The guarantee coverage ratio should also reflect the delivery method adopted: in the portfolio approach, the
guarantee coverage ratio should be lower than under the individual method, given that in the former the lender has an informational advantage as it retains the appraisal function. In our sample, we find limited evidence that the coverage provided under the portfolio approach is actually lower than the one offered on a loan-by-loan basis, except in Africa where the median difference between the coverage offered through the portfolio approach and the individual approach is 16 percent. Finally, the guarantee coverage ratio would be expected to be higher in countries with less developed financial sectors, in order to compensate for more pervasive market failures and imperfections. Surprisingly, we find that guarantee coverage ratios are on average more generous in high-income countries (median of 75 percent) than in developing economies (65 percent), probably reflecting a legacy of the global financial crisis, where many advanced economies stepped up the use of CGSs with very attractive terms which have not been phased out yet.

A very important feature of any CGS concerns the prudential regulatory recognition of the guarantee issued by the scheme. In most jurisdictions, the prudential regulation of lenders provides for a favorable treatment of exposures to the government for the purpose of calculating prudential capital requirements. This implies that the loans guaranteed by the CGS would benefit from lower risk weight or equivalent probability of default. Lenders would incur a lower cost of capital, raising significantly their incentives to participate in the scheme. However, the guarantee issued by the CGS should meet certain minimum legal requirements in terms of seniority, revocability, and effectiveness as specified by the financial regulator. We find that for 70 percent of the surveyed CGS, the guarantee provided to lenders does indeed qualify for the latter’s capital relief (Table 4). This is not the case in 20 percent of the CGSs in our sample, while another 10 percent are unaware of the prudential regulatory implications of their products. The guarantee issued by the CGS should also comply with relevant prudential regulation related to loan classification and provisioning rules so as to provide an additional incentive to lenders to participate in the scheme. We find results broadly similar to the previous topic, with one interesting exception: in almost half of CGSs in MENA, the guarantee provided by the CGS is not recognized for the purpose of estimating loan losses and provisions on bad exposures.

Appropriate pricing in another essential aspect of the CGS’ operational framework. The fees the CGS applies to the guarantees are important in shaping the incentives for lenders and SME borrowers, as well as for the financial sustainability of the scheme. For these reasons, the CGS should adopt a transparent and consistent pricing policy. Pricing should reflect the riskiness of the underlying loan portfolio. As per the basis to compute fees, this should always be the amount guaranteed. We find that the median annual fee levied by the CGSs in our sample is 2.4 percent (Table 4). Fees tend to be lower in Asia (median of 1.6 percent) and higher in in the Western Hemisphere, where they reach a median of 3 percent. Very few CGSs use a risk-based pricing structure: in only 39 percent of CGSs in our sample does pricing takes into account the historical performance of the guaranteed loans. The remaining 61 percent apply fixed fees across programs/products. Risk-based pricing is used by a majority of Asian CGSs (62 percent) while it is not implemented by any of the CGSs in MENA. Finally, more than half of the CGSs in our sample base the fees on the amount guaranteed, while 9 percent base it on the loan amount. Thirty-five
percent adopt a mixed approach, which in addition to the amount guaranteed and the size of the loan takes into account the maturity of the loan as well.

A final and often neglected area of the operational framework of a CGS is the overall claim management process. A CGS’s overall credibility depends to a large extent on how effectively claims are triggered and handled, whereas its financial sustainability can be enhanced through an efficient post-claim loss recovery process. The claim management process should be clearly and transparently documented in the legal agreements regulating the relationship between the CGS and the lender. To build and maintain lenders’ trust and avoid costly disputes, there should be a clear procedure for triggering a claim. All but two of the surveyed CGSs report that the contractual agreements with the lenders spell out the specific circumstances under which the lender can submit a claim. The trigger conditions for claims should specify the maximum period after a missed payment(s) and should not be conditional on initiating legal action against the SME borrower. While the median time after a missed payment(s) by the SME borrow that triggers a claim is 120 days in our sample, there is large regional variation. This ranges from only 30 days in Africa to 315 days in the Western Hemisphere (Table 5). In two-thirds of surveyed CGSs the lender can submit a claim before commencing any legal action against the defaulted SME borrower. However, in Africa this proportion is reversed.

Table 5
Claim management process

<table>
<thead>
<tr>
<th></th>
<th>Income Zone</th>
<th>Region</th>
<th>Western Hemisphere</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>All</td>
<td>High</td>
<td>Upper Middle</td>
</tr>
<tr>
<td># Days for submitting a claim (median)</td>
<td>120</td>
<td>120</td>
<td>105</td>
</tr>
<tr>
<td>Responsibility for debt recovery (%)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>CGS</td>
<td>64</td>
<td>30</td>
<td>4</td>
</tr>
<tr>
<td>Lender</td>
<td>19</td>
<td>57</td>
<td>70</td>
</tr>
<tr>
<td>Both</td>
<td>17</td>
<td>13</td>
<td>26</td>
</tr>
</tbody>
</table>

Once a claim is received, the guarantee payment should be settled in a timely manner. The legal agreements between the CGS and the lender should clearly state the conditions under which a claim is acceptable. The maximum amount of unpaid interest covered by the guarantee should also be clearly specified. In all but one CGSs in our sample, the conditions for making a payment are clearly detailed. The amount of unpaid interest due in the event of a claim is pre-agreed only in three-quarters of those CGSs which in addition to the principal cover also part of the unpaid interest.

The contractual framework regulating the guarantee agreement between the CGS and the lender should also indicate responsibilities for the loss recovery process. Yet 10 percent of surveyed CGSs, mostly found in Europe, do not have a clear post-claim recovery process. Because there may be economies of scale and scope in concentrating recovery activities in one organization, an ex-ante division of labor must also be clear between the CGS and the lender. In 64 percent of the schemes surveyed, the lender has the exclusive responsibility for pursuing the defaulted SME borrower, while in 19 percent it is the CGS which is in charge of recovery, a practice more commonly found in Europe and Asia. In the remaining 17 percent of CGSs in our
sample, recovery activities are jointly pursued by the CGS and the lender, indicating a duplication of work.

**III.D. Monitoring and evaluation**

Good practices identified in the fourth area of the Principles reveal how CGSs must report on their performance and, more importantly, evaluate the achievement of their policy objectives.

Timely and accurate financial statements are one of the most important tools for holding the management of an enterprise accountable for its stewardship of the company. CGSs are no exception and should produce annual financial statements at least annually. The financial statements should be prepared in accordance with the home country accounting standards required for domestic private sector financial enterprises. Using the same reporting standards as private sector enterprises allows the CGSs to draw on an established independent body of expertise for organizing and auditing their financial statements, as well as for evaluating their significance. Financial statements should be audited by a professional, certified audit firm. We find that 86 percent of surveyed CGSs produce periodic financial statements prepared on the basis of the standards applied to private sector financial institutions, and in all but two these are externally audited by an audit firm. However, 8 CGSs declared that they do not publicly report on their financial position and business activities. These CGSs are found in MENA and in the Western Hemisphere.

In addition to disclosing financial information, CGSs should also publicly report non-financial information. Such disclosure, often more qualitative in nature, can offer stakeholders key insights into the workings of the CGS and its prospects, as well as its relationship with the government. Non-commercial objectives form a fundamental part of the rationale for the existence of CGSs, and may have important repercussions for an individual PCG’s performance and viability and even for the fiscal position of the government. Therefore, it is essential that they are well defined and explicitly presented to the public. CGSs should disclose at least on an annual basis the social and economic commitments made, the social and economic outcomes of their activities, and any other relevant engagement. It turns out that non-financial information is publicly disclosed by three-quarter of surveyed CGSs, with no significant variation by level of economic development or region. Forty-five percent and thirty-nine percent of CGSs report commitments and outcomes, respectively, while 16 percent disclose other relevant non-financial information.

Another important piece of non-financial information disclosure of the CGS should be related to corporate governance, including board members background, retribution, board committee’s composition, etc. Where a mixed ownership model is adopted, the CGS should also disclose ownership structure and rights of minority shareholders, as well as any agreement between the government and private shareholders. In our sample, about three-quarters of CGSs disclose information related to their corporate governance. The most transparent CGSs from this perspective are based in Asia, where all but one CGSs report this information. A large majority of CGSs with private investors among their shareholders publicly disclose information related to
their ownership structure, rights of minority shareholder, special rights of the government, and any special arrangement such as a shareholders’ agreement.

A comprehensive and periodic evaluation of the CGS’s performance is necessary to account for the use of public resources, to measure the achievement of the CGS’ policy objectives, and to improve its operations. The CGS should establish a sound monitoring and evaluation system, and measure its performance at least every three to five years. This is the case for all but one CGSs in our sample. The performance of the CGS should be measured and evaluated along the dimensions of outreach, additionality, and financial sustainability, which correspond to the expected outcomes of a CGS. Outreach, or the capacity of the CGS to meet the demand for guaranteed loans by the SME target market, can be easily measured – it is typically proxyed by the number and volumes of outstanding guarantees – and this probably explains the fact that all but three surveyed CGSs declared that they systematically analyze their outreach.

It is more difficult to measure and assess the other two dimensions of CGSs’ performance: financial and economic additionality, and financial sustainability. The former refers to the impact of the CGS in terms of better quality and quantity of credit to SMEs, job creation, contribution to local economic development, etc. The latter concerns the ability of the CGS to sustain its operations on an ongoing basis with its capital endowment. Hence, an assessment of financial sustainability differs from simply reporting financial information as it requires a longer term perspective. We find that more than three-quarters of surveyed CGSs undertake an assessment of their financial and economic additionality as a part of their periodic performance measurement exercise. There is no significant variation among countries at different levels of economic and financial development, neither is there among regional groupings. This finding is quite surprising as one common criticism raised against CGSs is the lack of robust evidence on their additionality (Beck et al., 2010). We could not verify the methodologies employed by the surveyed CGSs to measure additionality; however, it is plausible that in many cases this is done by relying on the qualitative assessment of lenders and SME insiders to tell whether, for example, availability of credit to them has eased or jobs have been created (see Honohan, 2010). Depending on the design of the CGS and in particular on the nature of eligibility rules, it should be possible to use formal econometric methods to throw light on the question of additionality. We finally find that 85 percent of surveyed CGSs systematically measure and report on their long-term financial sustainability.

IV. Concluding remarks

CGSs have become an increasingly important policy tool through which governments around the world seek to address the issue of limited access to lending by SMEs. Unlike other types of interventions, such as state-owned banks or directed lending arrangements, CGSs typically combine a subsidy element with market-based credit allocation mechanisms. Therefore, they may generate fewer distortions in the credit market and may lead to better credit allocation outcomes. However, it is crucial that CGSs are operated to achieve outreach, additionality and financial sustainability.
To provide governments around the world with a set of good practices which can inform the design, implementation and evaluation of public CGSs, the World Bank Group and the FIRST Initiative, in partnership with international associations of CGSs and lenders, coordinated a task force of experts, which led to the drafting and dissemination of the Principles. This paper is a first effort to take stock of the level of implementation of the Principles. Using a survey of 60 public CGSs across 54 countries, it provides a first overview of how schemes perform vis-à-vis individual Principles based on a self-assessment provided by CGSs themselves.

Overall, our survey shows a fairly decent level of implementation of many individual Principles across countries in different income and regional groups. We find that surveyed public CGSs have in general a sound legal basis, with a clearly identified ownership entity, and their activities are supervised by a separate oversight body, typically the financial sector regulator. The CGS’s mandate is in many instances well defined and driven by clear eligibility rules. Most public CGSs adopt the individual approach to distribute their guarantees to partner lenders, though we find that the portfolio method is used more in developing countries. The claim management process is commonly well detailed in the relevant documentation. Surprisingly, we find that a large majority of surveyed CGSs systematically analyze their overall performance, including the additionality, though through qualitative assessments.

Our results also show weaknesses in several areas addressed by the Principles. The chartering legislation is silent on the sources of funding in almost a quarter of the CGSs in our sample. More than a third do not have minimum capital adequacy standards, mostly in high-income economies. For more than half of CGSs that are funded by subsidies there are no limits on budget appropriations. Mixed ownership, with private sector shareholders along with the government, is present only in 22 percent of the CGSs. The board appointment process, including qualification criteria for board members and representation from the private sector, is relatively weak in developing economies. We also find a relatively limited use of credit risk management systems, especially in developing countries, and risk management instruments to manage exposures. CGSs in general do not tailor the guarantee coverage ratio to their programs/products. In many jurisdictions the guarantee provided by the CGS is not given regulatory recognition for the purpose of calculating lenders’ capital requirements and for classifying and provisioning loans. We also find a low incidence of risk-based pricing. Finally, some CGSs do not publish financial statements and about one quarter do not disclose non-financial information.

While this paper is an important first step to shed light on the degree of implementation of the Principles for a large sample of public CGSs around the world, its findings should not be interpreted as a full diagnostic. The results of the survey are based on a self-assessment conducted by officials at CGSs on the basis of a simplified questionnaire drawn from the Methodology for Assessing Implementation of the Principles. No review of the legal environment and financial sector in which the CGS operates was undertaken. Moreover, no qualitative and judgmental analysis was carried out to qualify and contextualize the answers specific to individual Principles. These are critical steps to properly identify gaps where country authorities need to
focus their attention, and the World Bank Group stands ready to support its client countries in this effort.

As CGSs gain increasing interest and visibility as an important policy tool used by governments across the world to address the SME financial gap, more research is needed. First, more empirical work is required to better understand which specific CGS features work best in practice under which circumstances so as to prioritize interventions. Second, it would be important to conduct a proper cost-benefit analysis of public CGSs on the basis of a consistent and standardized analytical framework to ensure comparability of results over time and across countries. Both lines of research are in our agenda.
Acknowledgments

We would like to thank the FIRST Initiative for financial support and Abdul Abu Zaid for excellent research assistance. We are also especially grateful to Liudmila Uvarova for her help in designing the survey instrument. We are finally grateful to officials at public CGSs that completed the survey and at regional associations that helped with the process, as well as to Simon Bell, Steen Byskov, Lucia Cusimano, Eva Gutierrez, Jean Pesme, Roberto Rocha, Sebastian Schich, Moni Sengupta, Ghada Teima, Roya Vakil and participants to a World Bank Group seminar for useful comments. This paper’s findings, interpretations and conclusions are entirely those of the authors and do not necessarily represent the views of the World Bank Group, its Executive Directors, or the countries they represent.
References


Principle 1

The CGS should be established as an independent legal entity on the basis of a sound and clearly defined legal and regulatory framework to support the effective implementation of the CGS’s operations and the achievement of its policy objectives.

Principle 2

The CGS should have adequate funding to achieve its policy objectives, and the sources of funding, including any reliance on explicit and implicit subsidies, should be transparent and publicly disclosed.

Principle 3

The legal and regulatory framework should promote mixed ownership of the CGS, ensuring equitable treatment of minority shareholders.

Principle 4

The CGS should be independently and effectively supervised on the basis of risk-proportionate regulation scaled by the products and services offered.

Principle 5

The CGS should have a clearly defined mandate supported by strategies and operational goals consistent with policy objectives.

Principle 6

The CGS should have a sound corporate governance structure with an independent and competent board of directors appointed according to clearly defined criteria.

Principle 7

The CGS should have a sound internal control framework to safeguard the integrity and efficiency of its governance and operations.

Principle 8

The CGS should have an effective and comprehensive enterprise risk management framework that identifies, assesses, and manages the risks related to CGS operations.
**Principle 9**

The CGS should adopt clearly defined and transparent eligibility and qualification criteria for SMEs, lenders, and credit instruments.

**Principle 10**

The CGS's guarantee delivery approach should appropriately reflect a trade-off between outreach, additionality, and financial sustainability, taking into account the level of financial sector development of the country.

**Principle 11**

The guarantees issued by the CGS should be partial, thus providing the right incentives for SME borrowers and lenders, and should be designed to ensure compliance with the relevant prudential requirements for lenders, in particular with capital requirements for credit risk.

**Principle 12**

The CGS should adopt a transparent and consistent risk-based pricing policy to ensure that the guarantee program is financially sustainable and attractive for both SMEs and lenders.

**Principle 13**

The claim management process should be efficient, clearly documented, and transparent, providing incentives for loan loss recovery, and should align with the home country’s legal and regulatory framework.

**Principle 14**

The CGS should be subject to rigorous financial reporting requirements and should have its financial statements audited externally.

**Principle 15**

The CGS should periodically and publicly disclose nonfinancial information related to its operations.

**Principle 16**

The performance of the CGS—in particular its outreach, additionality, and financial sustainability—should be systematically and periodically evaluated, and the findings from the evaluation publicly disclosed.
## Annex 2 – Surveyed CGSs

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<th>Credit Guarantee Scheme</th>
</tr>
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</table>
Annex 3 – Questionnaire

1) Credit Guarantee Scheme Name

_________________________________________________

2) Address

_________________________________________________

3) City

_________________________________________________

4) Country

5) Year of establishment

_________________________________________________

6) Ownership structure [list ultimate government entity and other shareholders in % of capital held]

_________________________________________________

_________________________________________________

_________________________________________________

_________________________________________________

7) Number of employees

_________________________________________________

8) Lines of Business

Credit guarantees [please select all that are appropriate]

[ ] Credit guarantees to SMEs (i.e. portable guarantees etc.)
[ ] Credit guarantees to financial institutions
[ ] Counter-guarantees to other CGSs
[ ] Other - Write In: _______________________________________________________

Technical assistance [please select as appropriate]

[ ] To financial institutions
[ ] To SMEs
Training [please select as appropriate]

[ ] To financial institutions
[ ] To SMEs
Other: ________________________________________________

9) Volume of outstanding guarantees in 2014 [please select as appropriate]

Value [please insert value]: ________________________________________________
Currency [please specify currency]: __________________________________________

10) Number of guarantees issued in 2014

_________________________________________________

11) Number of SMEs served (directly or indirectly) in 2014

_________________________________________________

12) Total capital in 2014

Value [please insert value]: ________________________________________________
Currency [please specify currency]: __________________________________________

13) Volume of nonperforming guaranteed loans in 2014

Value [please insert value]: ________________________________________________
Currency [please specify currency]: __________________________________________

14) Number of nonperforming guaranteed loans in 2014

_________________________________________________

A. Legal and Regulatory Framework

15) Is the CGS established by law, decree or other relevant source of primary legislation?

( ) Yes
( ) No
16) Is the CGS established as an independent entity with legal personality?

( ) Yes
( ) No

17) If No, please select as appropriate

[ ] Program / Department of a government-owned development finance institution
[ ] Program / Department of a Ministry or government agency
[ ] Program / Department of the Central Bank
[ ] Other - Write In: ____________________________________________

18) If the CGS does not have legal personality:

Does the CGS have financial autonomy such as a separate capital and budget?

( ) Yes
( ) No

Does the CGS have operational autonomy such as dedicated governance body, management and staff?

( ) Yes
( ) No

Does the CGS have a specific operational framework different from the rest of the government agency?

( ) Yes
( ) No
( ) Not applicable

19) Does the legal and regulatory framework establishing the CGS indicate which ownership entity (ministry, agency etc.) represent the government?

( ) Yes
( ) No

20) If yes, please select as appropriate

( ) Ministry of Finance
( ) Ministry of Economy
( ) Ministry of Commerce and Industry
( ) Central Bank
( ) Other - Write In: ____________________________________________
21) Does the legal and regulatory framework establishing the CGS indicate the sources of funding of the CGS?

( ) Yes
( ) No

22) What are the main external sources of funding of the CGS? [please select all that are appropriate]

[ ] Subsidies and other budget appropriations
[ ] Government guarantees
[ ] Equity
[ ] Concessional loans from the government
[ ] Loans from other government agencies including development banks
[ ] Loans from private financial institutions

23) Is the CGS subject to a maximum leverage ratio (i.e. ratio of outstanding guarantees divided by total equity) as per the chartering legislation and/or regulation?

( ) Yes
( ) No

24) What is the maximum leverage ratio (i.e. ratio of outstanding guarantees divided by total equity)?

Indicate in %

( ) %: ____________________________________________
( ) Not applicable

25) If the CGS receives subsidies and other budget appropriations from the government, are there limits referenced or described in the relevant legislation?

( ) Yes
( ) No
( ) Not applicable

26) Are funding arrangements – including usage, existing limits on budget appropriations, subsidies, and government guarantees – reviewed periodically and audited by the Supreme Audit Institution or any other mandated institution in line with the country laws?

( ) Yes
( ) No

27) Does the CGS have minority shareholders from the private sector in its capital?

( ) Yes
( ) No
28) If Yes, please enter % of capital as of 2014

Financial institutions [please enter % of capital as of 2014]: ________________________________

SMEs and/or SME associations [please enter % of capital as of 2014]: ________________________________

Other [please enter % of capital as of 2014]: ________________________________

29) Does the legal and regulatory framework of the CGS expressly promote voluntary, minority participation of the private sector in the CGS capital?

( ) Yes
( ) No

30) Do minority shareholders have the right to actively participate in the governance and decision making process of the CGS through board representation etc.?

( ) Yes
( ) No
( ) Not applicable

31) Does the legal and regulatory framework mandate which body is responsible for supervising the CGS?

( ) Yes
( ) No

32) Who supervises the CGS? [please select all that are appropriate]

[ ] No one
[ ] Ministry of Finance
[ ] Ministry of Economy
[ ] Ministry of Commerce and Industry
[ ] Central Bank or Financial Regulator
[ ] Other - Write In: ________________________________

33) What is the scope of supervision? [please select all that are appropriate]

[ ] Determine that the CGS has a sound corporate governance framework?
[ ] Determine that the CGS has appropriate risk management strategies, policies, processes and limits?
[ ] Determine that the CGS has an internal process for assessing its overall capital adequacy in relation to its risk profile?
[ ] Take measures should the CGS raise above the maximum leverage (i.e. ratio of outstanding guarantees divided by total equity)?
[ ] Determine that the CGS has adequate policies and processes for identifying, classifying, provisioning and managing problem assets?

[ ] Ensure that the CGS performs only those activities which are explicitly listed in chartering legislation and fiscal budgets?

[ ] Other - Write In: ________________________________

[ ] Not applicable

34) Does the supervisor have the legal authority to enforce prudential standards and secure corrective measures when necessary, including formally raise objections and seek administrative injunctions of inadmissible activities?

( ) Yes

( ) No

B. Corporate Governance and Risk Management

35) Does the law or decree establishing the CGS prescribe a clear and explicit mandate for the CGS?

( ) Yes

( ) No

36) What does the mandate include?

[ ] The target SMEs

[ ] The main line(s) of business of the CGS

[ ] Other - Write In: ________________________________

[ ] Not applicable

37) Is there an explicit mechanism included in the legal and regulatory framework for periodically assessing the relevance of the CGS’ mandate?

( ) Yes

( ) No

( ) Not applicable

38) Does the CGS establish clear strategies tailored to its target sectors and groups?

( ) Yes

( ) No

39) Does the legal and regulatory framework establishing the CGS include a clear appointment process for the board of directors?

( ) Yes
40) Does the Board appointment policy specify minimum qualification criteria for its members?

( ) Yes
( ) No
( ) Not applicable

41) Are board members serving a fixed term?

( ) Yes
( ) No
( ) Not applicable

42) Does the CGS’ board include an independent and unaffiliated member(s) from the private sector?

( ) Yes
( ) No
( ) Not applicable

43) Does the CGS have an internal audit and compliance function?

( ) Yes
( ) No

44) Is the internal audit and compliance function authorized to conduct investigations at the request of the board or board committee?

( ) Yes
( ) No
( ) Not applicable

45) Does the CGS have a comprehensive enterprise risk management framework (i.e. including credit risk, market and liquidity risk, and operational risk) in place?

( ) Yes
( ) No

46) Is the enterprise risk management framework subject to board approval and its relevance periodically assessed?

( ) Yes
( ) No
( ) Not applicable
47) Does the CGS have a credit risk management system in place which relies on both quantitative and qualitative methods of analysis?

( ) Yes
( ) No

48) Does the CGS’ credit risk management framework include exposure limits by: [please select all that are appropriate]

[ ] Sub-sector of activity
[ ] Geographical area
[ ] Other - Write In: ________________________________
[ ] Not applicable

49) Does the CGS use credit risk mitigation techniques (i.e. co-guarantees, counter-guarantees etc.) to manage concentration risk?

( ) Yes
( ) No

50) If Yes, [please select as appropriate]

[ ] Counter-guarantees
[ ] Co-guarantees
[ ] Other - Write In: ________________________________

51) Does the CGS have accounting policies in place to properly value the outstanding guarantees?

( ) Yes
( ) No

52) Does the CGS have a framework to identify and manage environmental, social and corporate governance risks associated with its activities?

( ) Yes
( ) No

53) Does the CGS have a liquidity and market risk management framework in place?

( ) Yes
( ) No

54) If Yes, please select as appropriate

( ) Analysis of liquidity requirements?
( ) Contingency planning, for example, a concessional stand-by line of credit from the government?
( ) Other - Write In: ______________________________________________________________

55) Is there an investment policy that provides guidance on permissible investments of the CGS’s capital?

( ) Yes
( ) No
( ) Not applicable

56) Is there an operational risk management framework in place?

( ) Yes
( ) No

57) If Yes, please select as appropriate

( ) Codes of conduct rules and recruitment policies?
( ) Business resumption/continuity planning?
( ) Other - Write In: ______________________________________________________________

C. Operational Framework

58) How many programs/products is the CGS running?

______________________________________________________________

59) Does the CGS have clear eligibility rules for target SMEs?

( ) Yes
( ) No

60) Are eligibility criteria for target SMEs publicly available?

( ) Yes
( ) No
( ) Not applicable

61) Are eligibility criteria for target SMEs periodically assessed to ascertain their relevance?

( ) Yes
( ) No
( ) Not applicable
62) Does the CGS have minimum qualification criteria for partner lenders that are publicly available/communicated in advance?

( ) Yes
( ) No

63) What credit instruments does the CGS target?

[ ] Investment/long term finance [please insert the % of investment/long term finance of total outstanding guarantees]: ________________________________

[ ] Working capital/short term finance [please insert the % of working capital/short term finance of total outstanding guarantees]: ________________________________

64) What does the guarantee issued by the CGS cover?

[ ] Principal loan amount
[ ] Part of unpaid interest: ________________________________

65) What is the CGS’ delivery approach?

[ ] Individual/loan by loan approach [please insert the % of individual/loan by loan approach of total outstanding guarantees]: ________________________________

[ ] Portfolio approach [please insert the % of portfolio approach of total outstanding guarantees]: ________________________________

66) Under which circumstances is the individual approach adopted? Select all that are appropriate.

[ ] As the ordinary / default option
[ ] For relatively large loans
[ ] For relatively small loans
[ ] When there is emphasis on the specific project submitted by the SME borrower
[ ] Other - Write In: ________________________________
[ ] Not applicable

67) Under which circumstances is the portfolio approach adopted? Select all that are appropriate.

[ ] As the ordinary / default option
[ ] For relatively large loans
[ ] For relatively small loans
[ ] When there is emphasis on promoting a certain type of SME
[ ] Other - Write In: ________________________________
[ ] Not applicable
68) What is the guarantee coverage ratio?

<table>
<thead>
<tr>
<th></th>
<th>minimum %</th>
<th>maximum %</th>
<th>average %</th>
</tr>
</thead>
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<td>For individual</td>
<td></td>
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<td>guarantees</td>
<td></td>
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</tr>
</tbody>
</table>

69) Is the guarantee coverage ratio clearly specified in the contractual agreements between the CGS and the lender?

( ) Yes
( ) No

70) Is the guarantee coverage ratio set based on the SME targeted sectors and groups so that different coverage ratios apply to different programs/products?

( ) Yes
( ) No

71) Is the guarantee coverage ratio set based on the delivery approach employed by the CGS so that different coverage ratios apply for different delivery methods?

( ) Yes
( ) No

72) What kind of coverage does the guarantee provide?

[ ] Pari passu (shared equally between the CGS and the lender) [please insert the % of pari passu of outstanding guarantees]:

[ ] First loss [please insert the % of first loss of outstanding guarantees]:

73) Does the banking regulatory framework provide capital relief to lenders as a result of the usage of guarantees issued by the CGS?

( ) Yes
( ) No
74) Does the banking regulatory framework recognize the guarantee extended by the CGS for the purpose of loan loss classification and loan loss provisioning for collateralized assets by the partner lender?

( ) Yes
( ) No
( ) Don't know

75) What are the fees on the guarantees issued by the CGS?

minimum %: ________________________________
maximum %: ________________________________
average %: ________________________________

76) Are fees expressed as a fixed percentage or vary based on the riskiness of the beneficiary?

( ) Fixed
( ) Risk-based

77) Are fees levied on [select as appropriate]

[ ] Amount guaranteed
[ ] Size of the loan
[ ] Maturity
[ ] Other - Write In: ________________________________

78) Do the contractual agreements between the CGS and the lender clearly spell out the specific circumstances under which the lender can submit a claim?

( ) Yes
( ) No

79) Is there a maximum period after a missed payment(s) by the SME borrower a condition for submitting a claim?

( ) Yes, [please specify #days]: ________________________________
( ) No

80) Can the lender submit a claim to the CGS before commencing legal action against the SME borrower?

( ) Yes
( ) No
81) Do the contractual agreements between the CGS and the lender clearly describe the conditions under which a claim is acceptable and a payment can be settled?

( ) Yes
( ) No

82) Do the contractual agreements between the CGS and the lender specify the amount of unpaid interest covered by the guarantee issued by the CGS?

( ) Yes
( ) No
( ) Not applicable

83) Do the contractual agreements between the CGS and the lender clearly outline the post-claim loss recovery process?

( ) Yes
( ) No

84) Who takes formal responsibility for debt recovery? Select as appropriate.

[ ] CGS
[ ] Lender
[ ] Third party

D. Monitoring and Evaluation

85) Does the CGS publish financial statements at least on an annual basis?

( ) Yes
( ) No

86) Are the CGS’ financial statements prepared in accordance with the country’s accounting standards applied to domestic private sector financial enterprises?

( ) Yes
( ) No

87) Are the CGS’ financial statements externally audited by an audit firm?

( ) Yes
( ) No
88) Does the CGS publicly disclose non-financial information at least on annual basis?

( ) Yes
( ) No

89) If Yes, please select as appropriate

( ) Social and economic commitments made
( ) Social and economic outcomes
( ) Other - Write In: ____________________________________________

90) Does the CGS disclose information related to its corporate governance structure?

( ) Yes
( ) No

91) Does the CGS disclose its ownership structure, rights of minority shareholders and any special right retained by the government?

( ) Yes
( ) No
( ) Not applicable

92) Does the CGS disclose any shareholder agreement between the government and private shareholders?

( ) Yes
( ) No
( ) Not applicable

93) Does the CGS evaluate the performance of its operations at least every three to five years?

( ) Yes
( ) No

94) Does the performance evaluation of the CGS comprise an analysis of its outreach (i.e. number of guarantees issued and amount of outstanding guarantees to eligible SMEs)?

( ) Yes
( ) No

95) Does the performance evaluation of the CGS comprise an analysis of its financial and economic additionality (or impact of its operations)?

( ) Yes
( ) No
96) Does the performance evaluation include an assessment of its financial sustainability?

( ) Yes
( ) No