



## **URBAN DEVELOPMENT FUND**

**OPRG 2014 - 2020**

**Executive summary for discussion purposes only**

**February 2017**

Dear Partners,

We are pleased to present you the executive summary with respect to the Urban Development Fund financed by the Operational Programme Regions in Growth 2014-2020.

We strongly believe that an effective financial instrument should reflect the prevailing market conditions and be aligned with the requirements of its intended stakeholders.

Hence, we would highly appreciate any comments or recommendations you may have regarding the indicative structure of the instrument presented herein.

We look forward to working with you.

Kind regards,

FMFIB Management Board

## Background

- “Fund Manager of Financial Instruments in Bulgaria” EAD (FMFIB) has been appointed by the Managing Authority (MA) of Operational Programme “Regions in Growth” 2014-2020 (OPRG) to manage the financial instruments under the Programme
- This mandate incorporates *inter alia* the design and set-up of financial instruments providing loans and guarantees in the key sectors such as Urban Development, Energy Efficiency and Tourism and Cultural Heritage
- The total budget earmarked for the implementation of the UDF amounts to BGN 370 million

## Our role

- FMFIB is tasked with: (i) structuring the financial instruments in line with the objectives of OPRG; (ii) selection of financial intermediaries which demonstrate relevant experience to manage the funds; and (iii) monitoring the fund managers and the performance of the UDF over the course of the fund life

## Soft market test

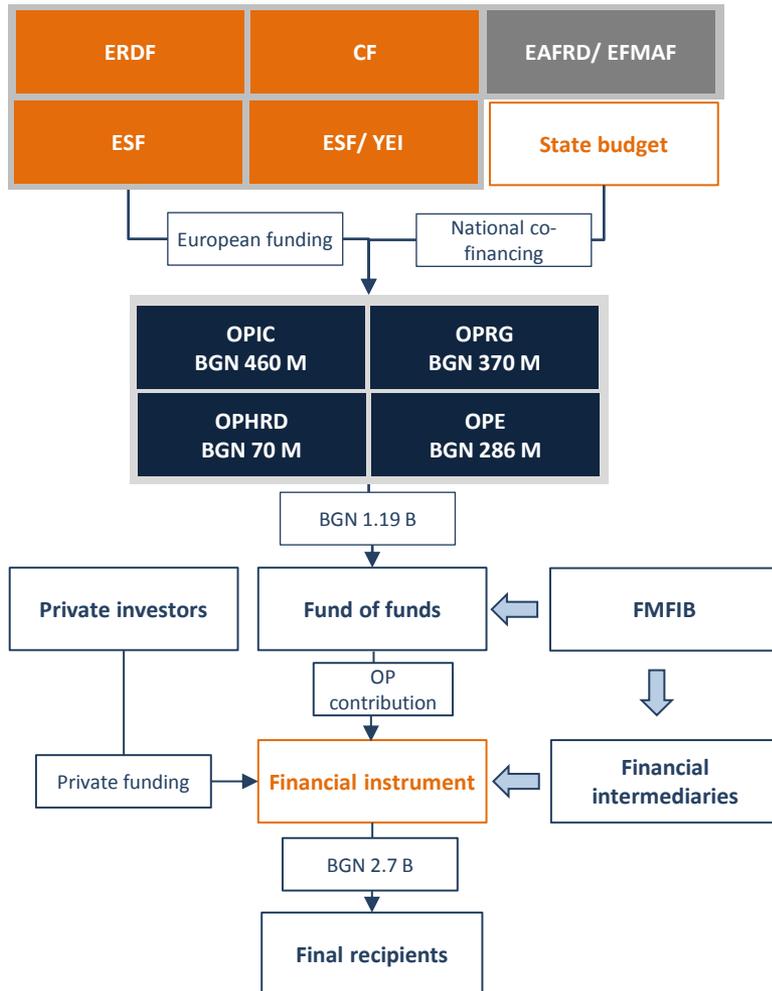
- FMFIB strives to execute its mandate efficiently and transparently. Hence, the design of our instruments should be aligned with the prevailing market practices
- In light of the above, we intend to conduct comprehensive consultations with the potential stakeholders in relation to UDF, including potential fund managers, commercial banks, private investors, consultants, etc.

## Purpose of this presentation

- The purpose of this summary (“the Document”) is to outline the tentative structure of the Urban Development Fund
- Furthermore, FMFIB has published an indicative term sheet which presents the key terms and conditions of the instrument to serve as a basis for discussions in the course of the market test

## Structure of this document

- The Document encompasses a high level overview of:
  - FMFIB structure, capabilities and role in the process
  - Background and policy rationale of the financial instrument
  - Main features and key indicative terms & conditions of the UDF
  - Tentative roadmap of the overall process up to the potential financial closing of instrument

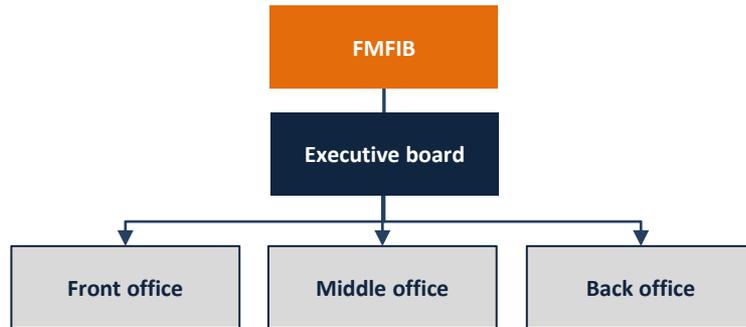


## Financial instruments background

- The EU has identified that the financial instruments (FIs) are an important instrument towards achieving its policy objectives
- By definition, the EU FIs are designed to support final recipients via market-driven mechanisms (such as loans, equity investments etc. as opposed to grants) while mobilising additional funds and expertise from the private sector
- The structure of the FIs also entails revolving of the deployed funds, i.e. would enable the reuse of public funds for the same policy goals
- Given their advantages over grants, the Union considers to channel an increasing portion of its budget to financial instruments

## FoF rationale

- Bulgaria has made a strategic decision to implement the FIs under its operational programmes (OPs) via a national investment scheme, i.e. the Fund of funds (FoF)
- Currently, four OPs pool their resources earmarked for FIs in FoF thus accumulating approximately BGN 1.19 billion
- The FIs are expected to mobilise support and additional capital from the private sector. Hence, the fully leveraged FoF is projected to facilitate investments in the Bulgarian economy in excess of BGN 2.7 billion
- FMFIB has been established by the government as the entity tasked with management of the FoF, where its corporate mission is the effective implementation of the national FIs
- The implementation of the FIs would be entrusted to intermediaries selected and monitored by FMFIB

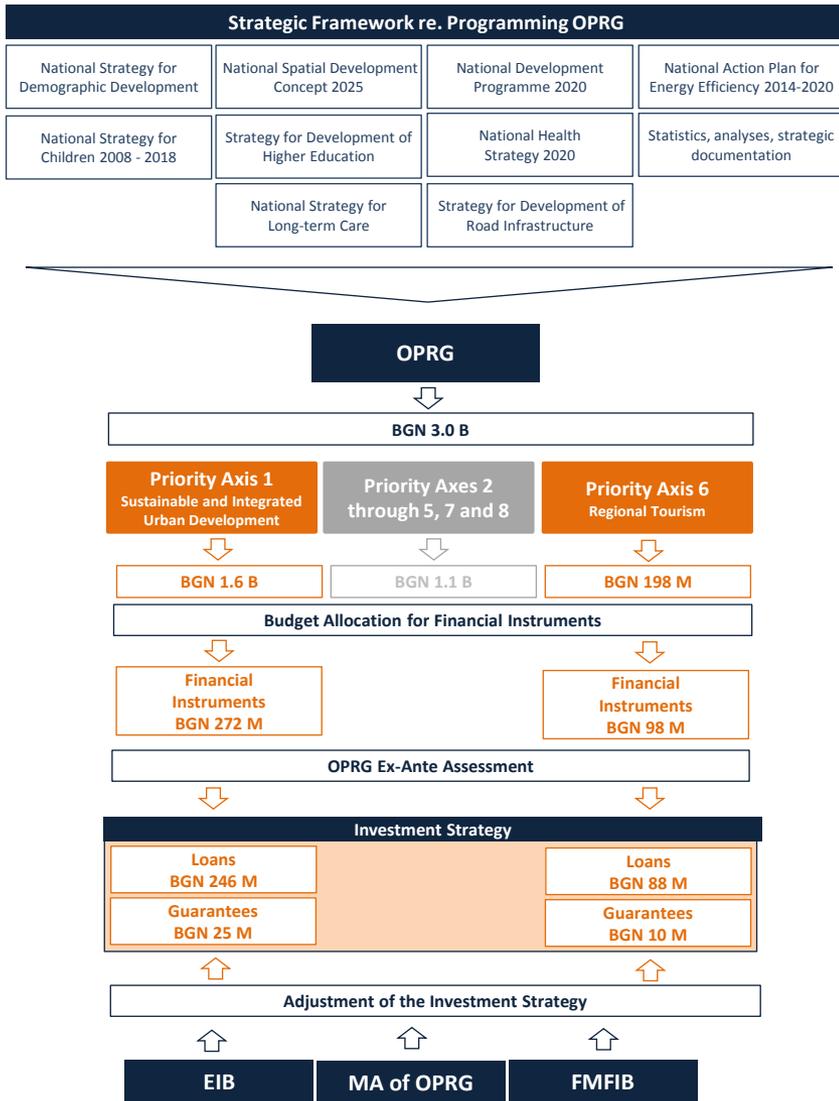


## FMFIB as FoF manager

- FMFIB was established in October 2015 and is operational since the beginning of 2016
- The governance as well as the *modus operandi* of the company have been designed with the advisory support of the EIB Group, EBRD and the World Bank
- Its management and internal control systems has been accredited by AEUF in May 2016
- FMFIB features a two-tier governance structure encompassing Supervisory and Management boards
- The Supervisory Board consists of representatives of the OPs funding the FoF and is chaired by a representative of the Ministry of Finance
- Our Management Board comprises of four seasoned professionals mobilising extensive experience in development and commercial banking, private equity as well as the public sector
- FMFIB has built a strong investment and operational team organised in three divisions as illustrated on the left hand graph

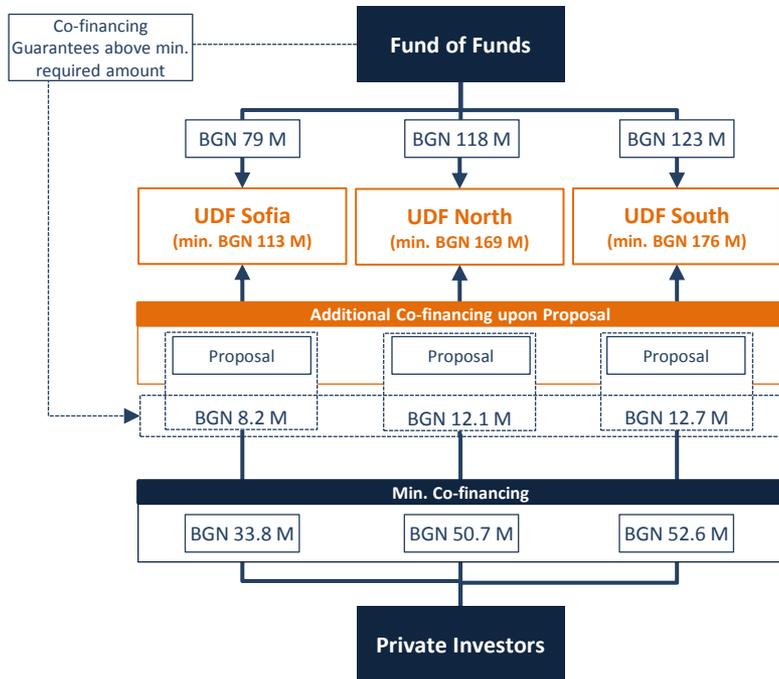
## Regulatory framework

- FMFIB duly complies with a number of European Union and national regulations, notably the CPR (EC) 1303/ 2013, the Bulgarian ESIF Management Act and the Public Procurement Act



## OPRG Funding and Objectives

- The Programme is funded by ERDF and national co-financing and has a total budget of approximately BGN 3 billion structured in eight priority axes
- The core principles of OPRG are aligned with the strategic framework, described on the left, that defines the national development roadmap in a number of sectors
- In the backdrop of these objectives and in view of the sectoral policies, the Programme resources should contribute towards the development of:
  - energy efficiency related to buildings and public transport
  - urban areas and tourism
  - social, educational and health infrastructure
  - regional road infrastructure
- The Programme envisages to support eligible projects and final recipients through grant funding and financial instruments, (loans, guarantees and/or a combination thereof)
- The practical implementation of the OP with respect to the FIs is outlined in an investment strategy, drafted by the EIB Group, which outlines the blueprint of FIs under OPRG



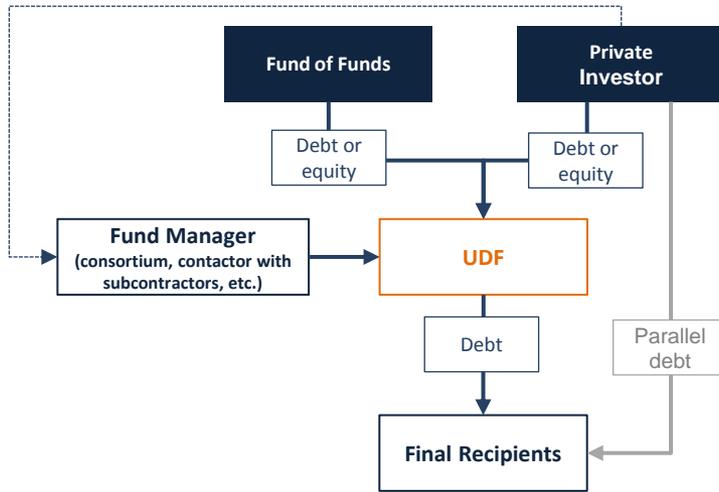
## UDF Rationale

- FMFIB would fund the UDFs to support projects in urban development, energy efficiency and regional tourism
- FMFIB would share the credit risk with the private investors
- The intermediaries should attract additional funding of minimum 30% of the total UDF size either on fund or on individual project level
- In addition, FMFIB would provide the possibility for guarantees partially covering the private financing which the UDF manager has attracted in excess of the required minimum of 30%
- The guarantee covers up to 80% of the additional co-financing above the required minimum on a individual loan level. The FMFIB exposure is capped at 25% of the theoretical maximal losses on portfolio basis (ref. to section Capped portfolio guarantee structure below)

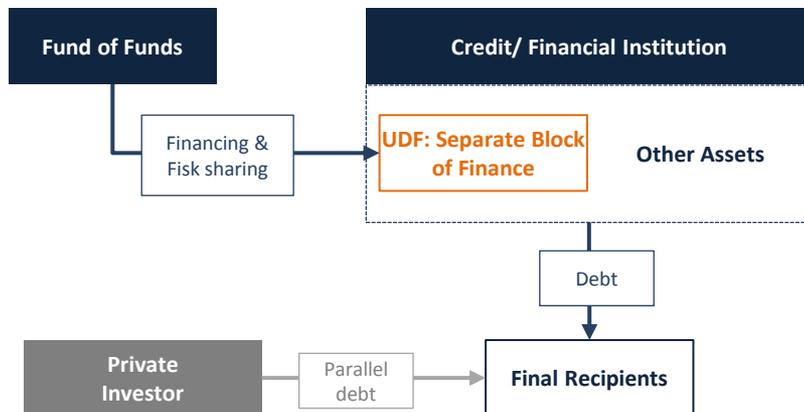
## Tentative design

- The design of the UDF comprises of the FoF, managed by FMFIB and three UDFs targeting different regions, namely Sofia, North Bulgaria and South Bulgaria.
- The UDF could be structured as a separate investment vehicle, a debt fund or as a separate block of finance, where both would be set-up and managed by the financial intermediary selected by FMFIB

## UDF implemented as a separate legal entity



## UDF implemented as separate block of finance



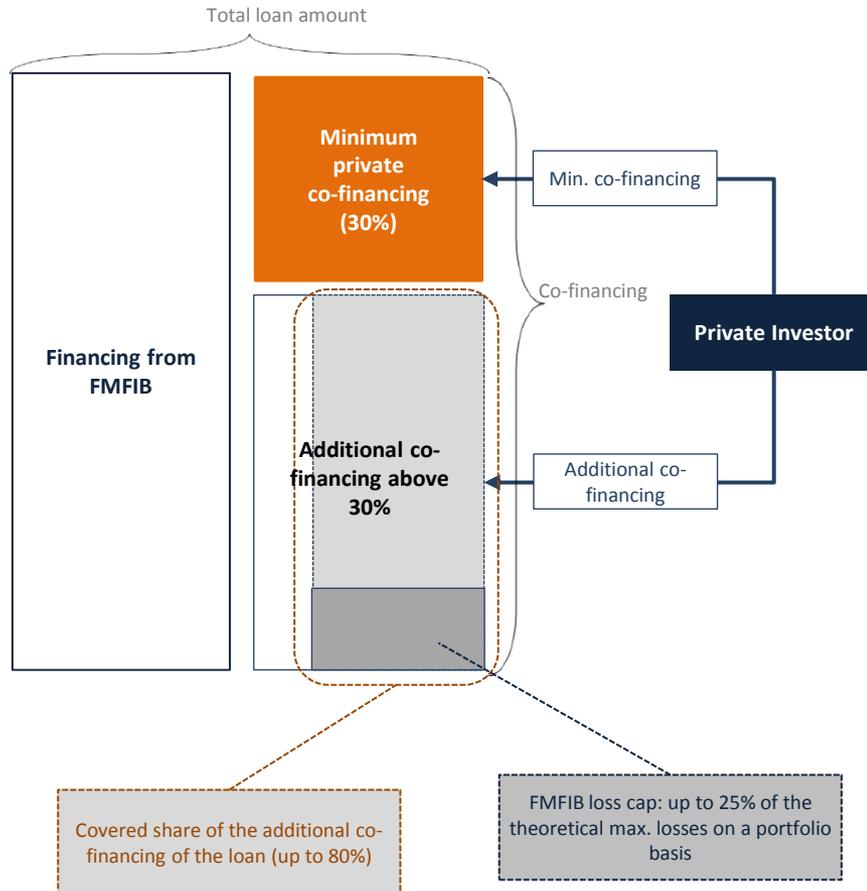
## Legal structure

- UDF could be structured as:
  - Dedicated legal entity, i.e. investment fund or
  - Separate block of finance
- FMFIB is considering to introduce eligibility criteria which entails a minimum credit rating of the financial institution wishing to implement the UDF as a separate block of finance
- The block of finance structure pertains separation of the UDF funds from the other resources of the institution in terms of governance, reporting, control mechanism, etc.
- The financing provided both by FMFIB or by private investors could be channeled to the UDF in the form of parallel debt at project level, debt, subordinated debt, equity or other type of investment as long as the public funds retain the pari-passu principle vis-a-vis the private ones

## Financial intermediary

- The selected financial intermediary could operate:
  - Individually
  - In a joint-venture with partner institutions
  - By retaining subcontractors (certain limitations under the Public Procurement Act may apply)
- The operational agreement with the selected bidder would set forth condition precedents in relation to the formal incorporation of the consortium and/or signature of the service contracts with the subcontractors

## Capped portfolio guarantee

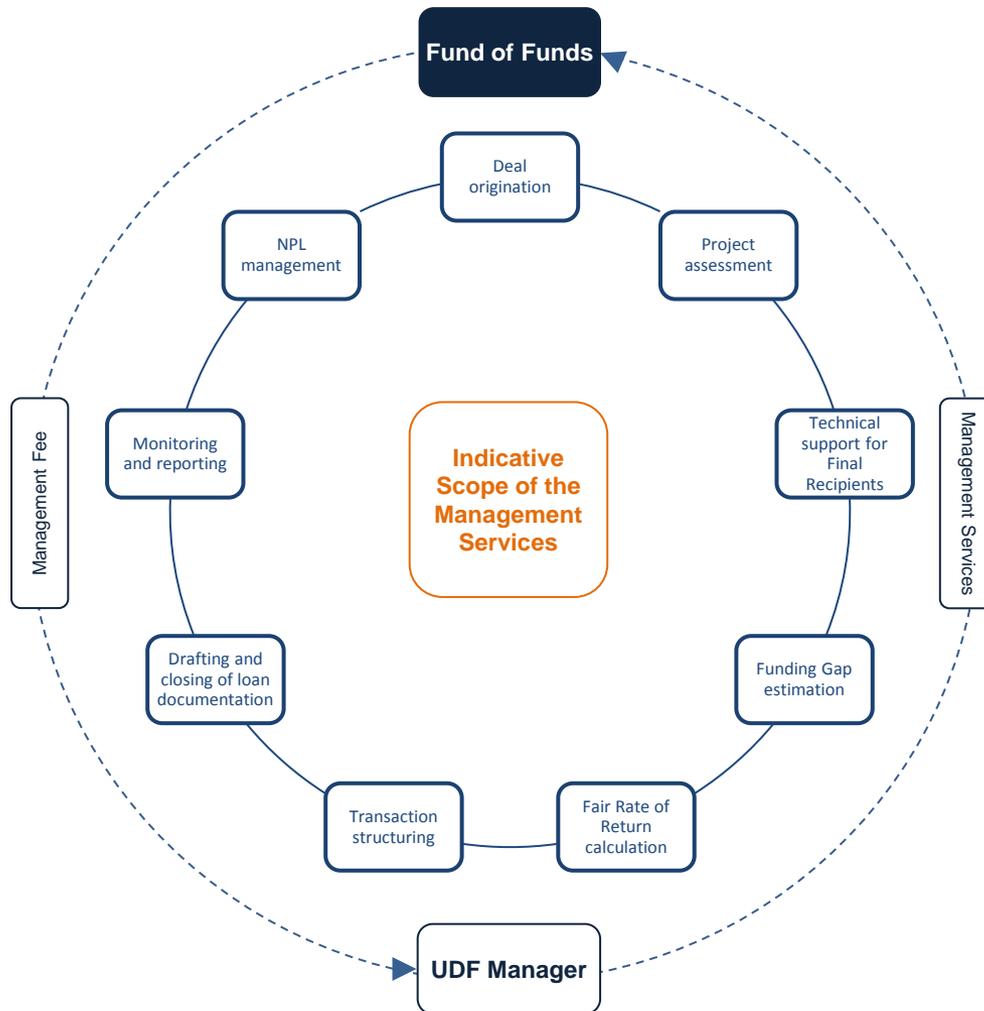


## Overview

- UDF could provide guarantees and/ or other credit enhancements in order to lower the credit exposure of the potential private investors
- If introduced, such instruments should support the intermediary to attract additional private co-financing in excess of the minimum requirement of 30% of the cumulative financial instrument

## Proposed guarantee structure

- At all times, the private investors should retain minimum 30% of the credit risk in each end project
- The guarantees would cover up to 80% of the provided co-financing above the minimum required amount
- FMFIB loss cap would be no more than 25% of the total guaranteed co-financing on a portfolio basis
- The loss cap rate would be set up on a case-by-case basis in the course of the selection procedure
- The chart illustrates the structure of the guarantee mechanism with 50% co-financing
- The indicative budget currently allocated for guarantees amounts to BGN 33 million for the three UDFs

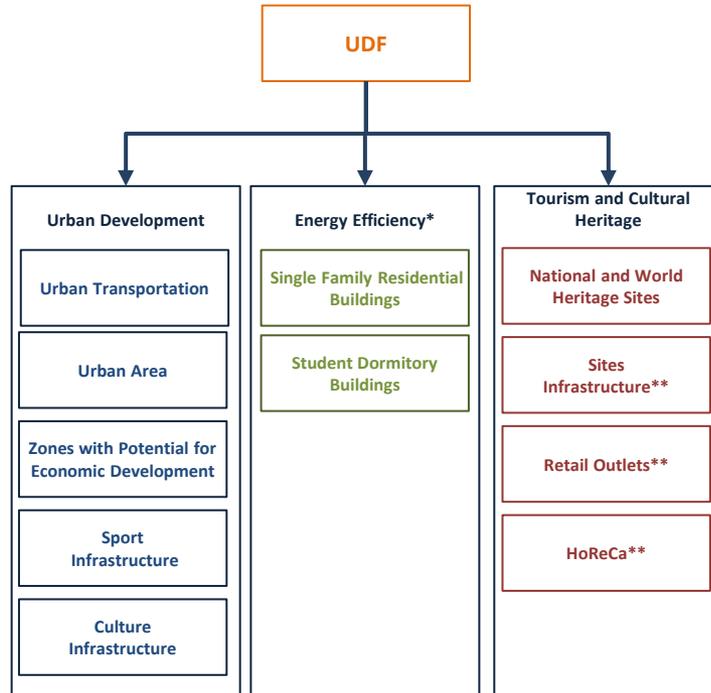


## Management Services overview

- The selected financial intermediary would provide integrated services including origination and management of the loan portfolio in compliance with the agreed investment strategy
- The scope of the management services would be defined in an operational agreement between FMFIB and the intermediary, whereas its execution would be aligned with the existing internal procedures and practices of the respective institution (if applicable)

## Management Fees structure

- The UDF manager would receive from FMFIB a two-tier compensation, as follows:
  - Basic component: percentage of the financing utilised by the UDF manager per annum
  - Performance Component: percentage of the FMFIB funds invested by the UDF Manager per annum
- FMFIB considers to introduce of a remuneration component based on the amounts paid back by the final recipients



\* According to the Programme structure, Energy Efficiency is a subcategory of Urban Development;

\*\* Shall be part of the respective national/ world heritage site.

## Urban Development

- The strategy of the financial instrument focuses on the development of both greenfield and brownfield infrastructure projects
- In order to be eligible for financing, the projects should comply with the Integrated Plans for Urban Regeneration and Development of the respective city
- Projects which include the development of functional connections with neighboring cities/ villages are considered as eligible investments
- Sport and culture infrastructure projects are also included in the scope of the investment strategy

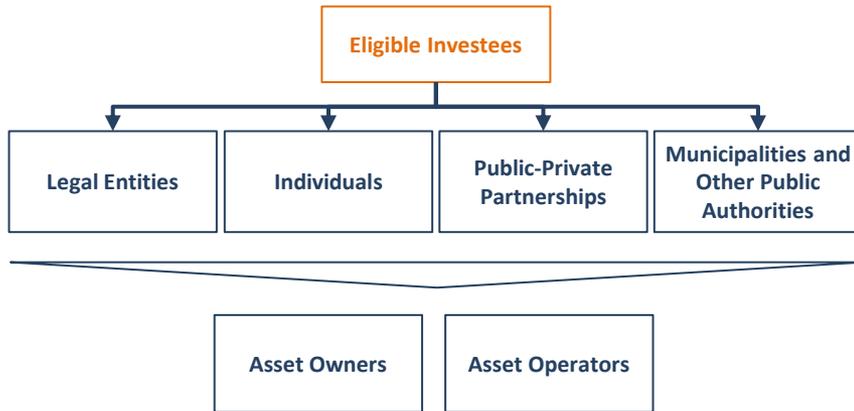
## Energy Efficiency

- The Energy Efficiency sector encompasses projects in single-family residential buildings and student dormitories
- Furthermore, provided that the project implementation achieves energy savings exceeding 60%, complete refurbishment and reconstruction is permitted
- Additional Energy Efficiency services may be covered, for instance energy efficiency audits and construction surveys
- Projects related to renewable energy installations are also eligible as far as they are utilised for own use

## Tourism and Cultural Heritage

- Projects involving cultural heritage sites of national and world importance listed into the National Registry of Immovable Cultural Heritage are eligible
- Activities which are not directly related to acquisition of tangible assets are also eligible, e.g. trainings and marketing campaigns, etc.

## Eligible Investees



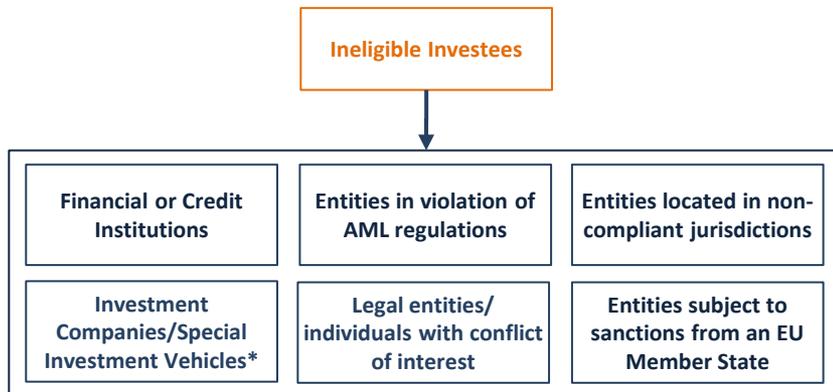
## Common requirements for Investees

- Final recipients should have the appropriate legal status to be eligible to apply for loans and implement projects
- The investees should have an adequate legal interest in the assets they invest in
- The projects should fall within the territorial scope of the relevant UDF

## Energy Efficiency Investees

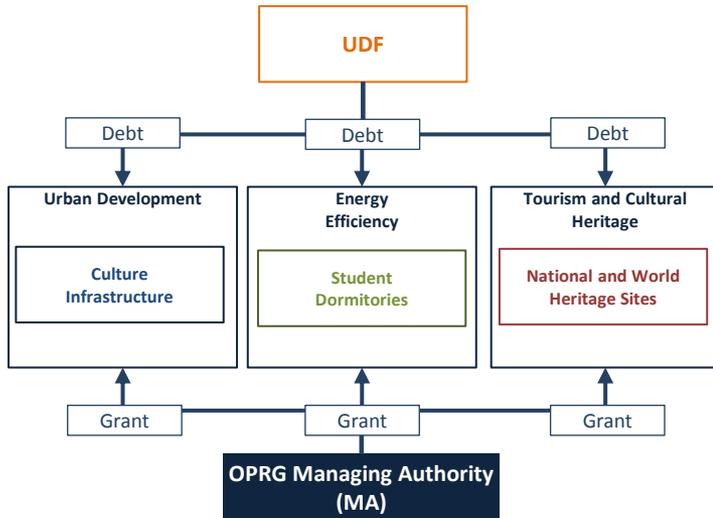
- Single-Family Building Owners
- Higher education institutions and legal entities managing student dormitories

## Ineligible Investees



\*SPVs, founded for a specific project are eligible

## Scope of the Combination among Sectors



## Overview

- UDF financing might be combined with grants when the eligible projects do not have the potential to generate sufficient revenue to service the loan

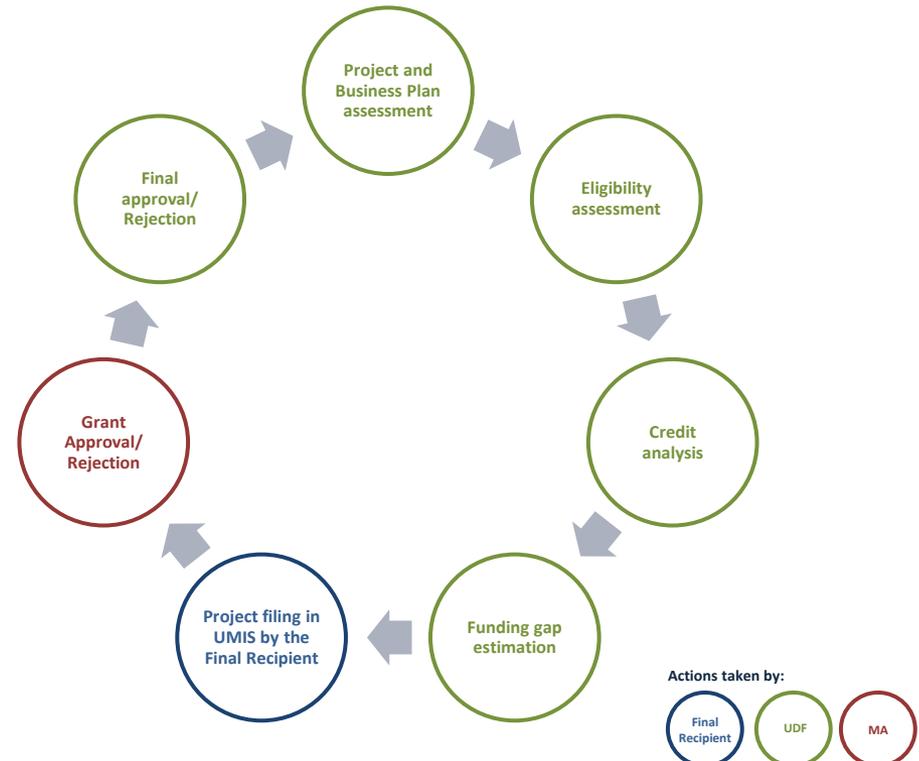
## Grant Combination Requirements

- Grant financing should not be used for loan repayment
- UDF financing can not be used to pre-finance grant
- Combination requires a clear separation between eligible activities and expenditures financed respectively with UDF loan and grant

## Financial Intermediary Involvement

- The Fund Manager plays a crucial role in the determination of the funding gap, i.e. the grant requirement
- Once eligibility and viability of the project are assessed the intermediary estimates the funding gap between expected proceeds and the projected debt service

## FI and Grant Combination Process

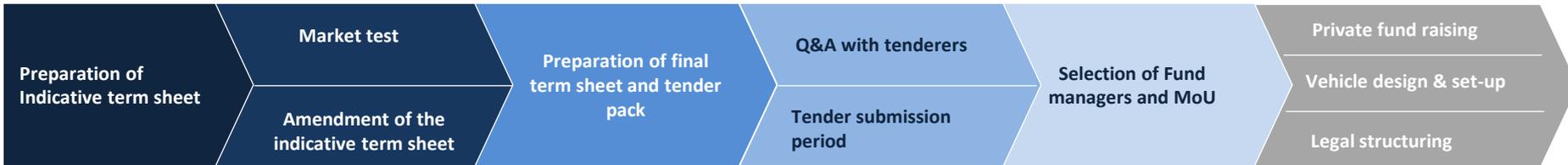


Feature	Description
<b>Type</b>	Investment loan, working capital financing, leasing, incl. combination thereof
<b>Amount</b>	Urban Development and Energy Efficiency: up to EUR 20 M Tourism and Cultural Heritage: up to EUR 10 M*
<b>Currency</b>	BGN / EUR
<b>Purpose</b>	Building or acquisition of long-term assets, working capital, VAT
<b>Down payment</b>	Min. 15% (5% and respectively 0% in specific cases)
<b>Term</b>	From 12 to 240 months (depending on the sector)
<b>Grace period (re. principle)</b>	Up to 36 months (depending on the sector)
<b>Interest rate</b>	Co-financing: 3m SOFIBOR + fixed allowance (according to the financial intermediary tender offer) FMFIB financing: % from the co-financing rate (according to the financial intermediary tender offer)
<b>Fees</b>	No fees shall be charged to the final recipients as far as the respective costs are covered by the management fee paid by FMFIB Commitment or Prepayment fees are permitted
<b>Penalty interest rate</b>	According to common practices of the fund manager
<b>Collateral</b>	According to the internal procedures and the tender offer

\*Applicable to World Heritage Projects

## Process Overview

- FMFIB would structure and conduct tenders for the selection of UDF managers
- The procedures would adhere the principles which pertain an open, non-discriminating, transparent and avoiding any conflict of interest process in accordance with applicable regulations
- The evaluation of the candidates would be performed by FMFIB, according to preset exclusion, selection and award criteria as described in the tender documentation
- The potential UDF Managers might express their interest towards more than one UDF. Nevertheless FMFIB is considering to introduce limitation regarding the number of funds managed by a single tenderer
- Most likely, the tender would be performed according to the two-stage procedure illustrated below



## Stage I

- Submission of EoIs and shortlisting
- FMFIB reserves full rights to review the declared technical abilities in the offers
- Shortlisted candidates would participate in the consecutive stage by submitting their initial offers

## Stage II

- The participants selected to proceed in the second round submit technical proposals which encompass, *inter alia*, business plan and investment policy and a pricing bid
- FMFIB would conduct rounds of negotiations with the eligible tenderers on predefined elements of the documents

## Opinion. Investment recommendation. Advice

This Investment opportunity outline (“the Document”), in whole or in part, is not to be construed as an opinion, or an investment recommendation, or a recommendation, or an advice to proceed or not with any considered transaction or other course of action.

According to the applicable regulations, the selection of financial intermediaries with respect to the implementation of the financial instruments under OPRG is subject to successful completion of a formal tender procedure and decision of FMFIB’s competent authorities.

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