AmCham EU

AmCham EU's position on the European Fund for Strategic Investments

Executive summary

Productive public investments and effective policies that promote private investments are key enablers of growth and competitiveness. AmCham EU therefore supports a swift adoption of the European Fund for Strategic Investments by the co-legislators, coupled with a non-politicised governance system that will send the right signals to private investors. AmCham EU is convinced that effectively managing prioritisation processes for competing projects will be paramount to the Fund's success. Our member companies look forward to a constructive debate on a genuine European investment funding strategy to help bridge the infrastructure-financing gap and to support sustainable growth and jobs.

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AmCham EU speaks for American companies committed to Europe on trade, investment and competitiveness issues. It aims to ensure a growth-orientated business and investment climate in Europe. AmCham EU facilitates the resolution of transatlantic issues that impact business and plays a role in creating better understanding of EU and US positions on business matters. Aggregate US investment in Europe totalled €2 trillion in 2014 and directly supports more than 4.3 million jobs in Europe.

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POSITION PAPER

22 June 2015

Introduction

The American Chamber of Commerce to the European Union (AmCham EU) has long highlighted the importance of productive public investments and of effective policies that promote private investments as key enablers of growth and competitiveness. The investment plan proposed by the Juncker Commission and the supporting legislative proposal for the European Fund for Strategic Investments (EFSI) were rightly established as one of the first priorities of the new European executive for growth and jobs. A well-functioning EFSI will be crucial to contributing to the delivery of the estimated €1.5 to €2 trillion infrastructure investment needed across Europe. The plan can also help support other important policy priorities defined under EFSI, such as energy efficiency.

AmCham EU therefore supports a swift adoption of EFSI by the co-legislators, coupled with a non-politicised governance system that will send the right signals to private investors. AmCham EU members are convinced that effectively managing prioritisation processes for competing projects will be paramount to the Fund's success. The following paper outlines our recommendations to enable the implementation of EFSI by the summer, as called for by Jean-Claude Juncker, Commission President, and to best leverage European funds within this framework. Our member companies look forward to a constructive debate on a genuine European investment funding strategy to help bridge the infrastructure-financing gap and to support sustainable growth and jobs.

1. Safe and modern infrastructure with smart funding

AmCham EU welcomes the recognition of energy, transport and communication infrastructure as a core enabler of the competitiveness of the European economy and looks forward to the implementation of the right tools and frameworks to nurture sustainable growth and jobs.

The time is right for a new deal on infrastructure investment in Europe

AmCham EU is convinced that further infrastructure investments can no longer be delayed if we wish to maintain and expand Europe's infrastructure at a time when global competitors race ahead to build the growth enablers of tomorrow. Investments in well-functioning energy, transport and communication systems that have adequate connections, reduce congestion and enable innovation should be accelerated. These investments would spearhead recovery efforts, as they open markets and can create jobs, bring cohesion, build lasting assets, enhance global competitiveness and improve the EU's attractiveness for industrial investment.

Over the past number of years, AmCham EU has shared its **concerns over the slow rate of engagement of infrastructure related investments within Europe.** Public and private investments, notably in the Eurozone, have been affected by a systematic decline during the last few decades, in conjunction with a slowdown in productivity and a decline in economic growth rates. During the crisis, several Member States cancelled or delayed major infrastructure projects. This puts at risk the many factors that make Europe a great place in which to do business and maintain a high standard of living. Reacting to the crisis, European governments chose a rather modest set of national stimulus plans to promote growth, directing on average only 0.3% of EU gross domestic product (GDP) toward public investment, in which infrastructure is included.

As a result of the crisis, budget consolidation remained necessary in many Member States. Projects were further delayed because of the pressures facing government budgets, at a time when 'productive' public and private expenditure should have stimulated higher rates of growth in the longer-term. This environment further influenced the 2014-2020 multiannual financial framework discussions – which should have focused more on seeding growth to avoid a 'lost decade' scenario. As a result, the proposals for a Connecting Europe Facility and other headings linked to infrastructure investment were significantly reduced, although we welcome that the remaining commitments still represent, in some cases, a significant improvement over the previous multi-annual frameworks.

The European Commission has acknowledged the very substantial needs for infrastructure funding over the next decade for Europe's networks, with estimates ranging between €1.5 trillion and €2 trillion until 2020. There is no shortage of investment opportunities to implement European goals and strategies, but there is also no shortage of global competition. Many of Europe's trading partners invest in the development of their infrastructure and compete through many initiatives for access to finance and to increase their attractiveness for foreign investment.

Clearly, **the EU's ability to deliver the necessary investments will be the real marker of a successful EU policy**. The alternative would most certainly lead to higher-cost solutions in the future. In this area, the **effective management of the prioritisation processes** for competing infrastructure projects as well as a balanced approach to permitting procedures supporting sustainable development is paramount to success.

We believe that **the time is right for a new deal on infrastructure investment in Europe** – both across the Union and at a national/regional level – leveraging the size of the EU and its Single Market, optimising the tools and resources already designed and available, and making the best use of record levels of individual savings and financial market conditions. This task includes building the missing infrastructure, implementing the multi-modal links and connections, removing bottlenecks and modernising existing infrastructure.

There are no free solutions, new sources of financing are required

AmCham EU shares the view that **sustainable growth cannot be built on ever-growing mountains of debt**. There is no doubt that, within the framework of rules set under the Stability and Growth Pact, the EU institutions and its Member States must pursue the strongly needed structural reforms and deliver on the consolidation of public finances through decisive and courageous actions. However, difficult decisions to reduce and control public spending should also be balanced and rewarded by efficient and smart investments to seed sustainable growth.

New sources of financing are required in order to meet the energy, transport and communication infrastructure needs. Back in 2010, we very much welcomed the development by the previous Commission of new financing sources, such as European project bonds and Public Private Partnerships for major European infrastructure projects. We supported the creation of infrastructure funds using several existing instruments to build a genuine European funding strategy through the Connecting Europe Facility. The experience gained in the European Investment Bank and other partners for infrastructure project financing should be fully leveraged. Risk sharing mechanisms, subordinated debtors and credit enhancement techniques offer vast potential.

AmCham EU strongly welcomed the commitment from Jean-Claude Juncker, Commission President, to present an ambitious Jobs, Growth and Investment Package within the first three months of his mandate, with a **strong focus on additional investment in infrastructure**. We called on the European Parliament and the Council to reach a timely agreement on the Commission's proposal for EFSI. We were pleased to see that economy and finance ministers endorsed EFSI, supporting a non-politicised governance system that will reassure private investors. We hope that close cooperation with the European Parliament will enable the implementation of EFSI by the summer, as called for by Jean-Claude Juncker.

AmCham EU, however, continues to stress that these new developments can only be valuable additions to the toolbox and not a substitute to structural issues. They **cannot replace the Member States' responsibilities to maintain a high level of productive public investment and adopt appropriate policies to stimulate private investment,** to move forward in implementing much-needed structural reforms. Europe needs an overall strong commitment to fund the initiatives it jointly decides upon and to deliver results. As such:

- The completion of **Trans-European Networks** should be backed by adequate budget prioritisation at European and national levels;
- Major investments are needed in the **internal energy market's hardware** in generation, networks and energy efficiency;
- A **strong regional policy** should continue to improve European cohesion through well-managed structural funds;
- Based on the successful impact of the €10 billion **capital increase of the European Investment Bank** (EIB) engaged in the past years, a further increase in the EIB's capital could be considered;
- When infrastructure usage charging schemes or taxation plans are developed, the **earmarking of revenues** generated from the use of infrastructure should be the rule and must contribute to secure adequate infrastructure funding.

Prevent market distortions

As the Commission rightly identified, the market for infrastructure financing is a very complex construction with specific requirements and long-term needs. The financial crisis also had a clear impact on investor behaviour and on the attractiveness of several instruments and markets.

All efforts should be geared towards fully understanding the specificities of infrastructure financing and assessing the impact of new sources of financing. In any case, **the introduction of new tools should not lead to financial market distortions or market access restrictions.**

In parallel, the further development of **a genuine European infrastructure funding strategy should not lead to the introduction of forced shifts between energy sources or transport modes.** AmCham EU strongly believes that any policy must be cross-modal in design, since modal shift is neither possible nor suitable in the very large majority of traffic or energy flows. On the contrary, effective co-modality allows the full supply chain – including customer expectations – to be considered, while each transport mode or energy source competes fairly on the basis of its own advantages and challenges.

Infrastructure charging and taxation should allow all transport modes and energy sources to be developed fairly in order to make co-modality work effectively in the transport and energy mix and to ensure mobility and energy security. It is crucial that earmarking provisions shall guarantee that *i.* 100% of the revenues are invested in measures to decrease the external costs of that particular transport or energy mode, and *ii.* that there is transparency in the use and deployment of these revenues. It is also important to promote innovation by ensuring technology neutrality. The market should decide the best new solutions to solve current challenges with the help of intelligent systems and facilitated by harmonised standards and administrative procedures.

A large part of the infrastructure also needs to support the greening of the economy and the move towards decarbonising transportation and energy supply. Rather than penalising, policies and measures should **encourage and reward actions that reduce absolute carbon emission levels.** Moreover, regulatory uncertainty regarding carbon emissions means that investors can be discouraged from making the necessary improvements and investing in the infrastructure to support new technologies. Policymakers, market players and researchers should act together to research and identify the most promising alternatives. This could entail financing through instruments such as an innovation fund at the EU level.

2. The external dimension

While the massive under-investment in infrastructure development is a critical challenge for Europe to develop growth and jobs within the Single Market, European institutions and Member States should not underestimate the need to **build stronger connections with the Union's global partners** through infrastructure investment. The development of infrastructure connections with and through **strategic third countries** clearly has a huge impact on Europe's access to raw materials and ability to trade in the global economy while leveraging global supply chains. Infrastructure is a significant dimension of the European Union's External Action.

Without continued support for infrastructure investment (notably through the instruments for pre-accession assistance, the funding and technical assistance tools or development banks), the **enlargement process** will be made much more difficult for accessing and candidate countries that have to demonstrate they will be able to play their full part as potential members of the European Union.

In addition, infrastructure investment remains at the heart of a successful **European Neighbourhood Policy,** especially to bring Eastern European partners closer to the EU through the Eastern Partnership and to further promote economic integration and democratic reform to the EU's south through the Euro-Mediterranean Partnership.

Infrastructure investment must also remain one of the core intervention areas embedded in the EU's **development policies**, and supported by the relevant funding. Better transport, sanitation, energy and communications systems contribute to the development of local capabilities. Poor infrastructure hampers growth and the ability of many developing countries to trade in the global economy and improve the standard of living for their populations.

3. Recommendations to maximise the efficiency of the Commission's investment plan

The creation of EFSI within the EIB - with its guarantee of €16 billion under the EU budget and €5 billion of EIB resources – is aimed at providing a €315 billion funding capacity that could make a meaningful impact. Whether the assumed multiplier of private capital is reasonable will, to a large extent, depend on the effective operation of EFSI. The efficiency of the Commission's investment plan can be maximised within the current funding arrangement. In this context, a crucial role will be played by the European Investment Advisory Hub and the European Investment Project Pipeline.

Transparency and predictability

- The approval process should be transparent and user-friendly, so that equity and debt investors know how to use the scheme or how long it takes to obtain approval. This will help them to reliably predict the outcome.
- The scheme should be able to respond in a reasonable time; e.g. two weeks for an initial review and six to eight weeks for a final approval – subject to receiving the appropriate information.
- Market participants should also understand how projects will be prioritised within the scheme, especially if a large number of projects fit the investment criteria.
- Clear guidance should be provided on which projects would be funded via the 'usual' route of the EIB's Project Bonds Credit Enhancement (PBCE) scheme and which projects will be financed by EFSI.
- Finally, since many projects are tendered under EU procurement rules, guidance on how EFSI would operate within such a process would be particularly helpful.

Documentation and associated risks

- With regards to public tenders, EFSI could bring consistency and discipline to the market, by ensuring that procuring bodies include basic 'bankability' terms in the project's documentation. This could be a role for the European Investment Advisory Hub.
- Where transaction documentation falls short of market standards, AmCham EU would recommend that EFSI offers risk mitigation to protect investors. In general, we would recommend that the Fund offers political risk insurance (e.g. to cover a breach of contract by Member States under a concession agreement). This would in part replicate products available from the Multilateral Investment Guarantee Agency (MIGA), but having a European-centric offering would be useful. This insurance should include political events prior to the completion of a project.
- In any case, to help market participants, we recommend providing guidance on exactly what each risk mitigation measure offered under EFSI will involve, including the key terms.

Project Pipeline

- To enable the targeted €315 billion funding to be optimally deployed, providing investors with a clear, searchable pipeline of credible opportunities will be of crucial importance. The Project Pipeline and the European Investment Advisory Hub are therefore key elements of the legislative proposal.
- It is important that the Project Pipeline would not simply be a list of all possible projects from individual Member States, but a vetted list of projects that should be acceptable to EFSI and would be quite likely to attract private capital.
- We note that the added value of the Commission's investment plan lies in enabling viable or partially viable projects. We define viable projects as projects that will go through with or without PBCE or EFSI assistance. The extra support may change the cost of capital, but not whether the project is financed or not.
- There is a relatively small universe of projects that could be categorised as 'potentially viable'. These cannot quite find private capital demand as they are, but could be financed with credit enhancement or risk mitigation. Today, these would be mainly located in peripheral Europe, where some investors may draw comfort from having the PCBE or EFSI involved. A specific example would be a case where a project would be categorised as sub-investment grade and hence have a higher cost of capital. Such projects would often not be executed, as the awarding authority is likely to seek terms consistent with an investment grade profile. Credit enhancement could offer a solution here.
- It is important to note that EFSI is not likely to change the execution of so-called 'unviable projects'. These are projects that cannot be financed due to significant issues with the terms, cashflows or risks. Credit enhancement is unlikely to make enough difference here. This is where the role of the European Investment Advisory Hub will be crucial. The Hub can help structure a project so that it produces suitable cash flows and contains acceptable risk sharing between the parties. This, however, also requires political willingness and continuity at the domestic level. Policymakers should therefore take a broad approach towards infrastructure finance, which addresses the entire political, financial and legal spectrum. A non-politicised governance system will help reassure private investors.

Gaining momentum

In the case of the PBCE, it has taken about two years to get a number of deals into the market. If EFSI is to move more rapidly, it will be important to start off by presenting a short initial list of well-defined and deliverable projects that meet all the criteria. This will help to familiarise investors with the process. It will, however, likely be a learning process, so gaining momentum could take a little time.

Once interest picks up, the Project Pipeline could be quickly expanded under the following conditions:

- The European Investment Advisory Hub should publish detailed guidance on the kind of deals it can support, so that Member States can appropriately assess their own pipelines.
- The Hub should publish detailed guidance on best practice for contractual terms, including risk sharing, so Member States can ensure projects are drafted in a viable manner.
- The European Investment Project Pipeline should provide a constructive vetting of projects, to ensure the Pipeline reflects 'real deals' only. This will encourage Member States to develop projects on terms that will be acceptable to EFSI.
- To set an example, EFSI could publish a list of 'pre-approved' projects that are 'shovel-ready' and would have EFSI support.

Investor base

- Under the conditions mentioned above, the Commission's investment plan will raise the profile of infrastructure finance and will attract potential investors. We expect that the plan could draw in smaller investors in particular. These investors typically lack the in-house knowledge to invest in infrastructure projects and are therefore currently absent from this market. They will likely appreciate the EU support and credit enhancement, especially while they familiarise themselves with this sector.

4. Future options to increase the funding capacity

Once the Commission's investment plan has fulfilled its potential, policymakers may wish to consider innovative ways to further enhance its funding capacity. To this end, AmCham EU provides further recommendations:

EFSI is currently set as a separate account within the EIB. This structure limits the plans's capability to act boldly while EFSI could also work for higher risk initiatives, which will be most relevant to the private sector. At a later stage and leveraging initial success, **the creation of a separate legal entity/agency which would fund itself directly on the market could be explored**. This agency could have a legal and governance structure very similar to the European Stability Mechanism (ESM). It would be capitalised by the 28 Member States, which contribute proportionally to their GDP, under several but not joint liability. The bonds issued by the agency would attract a broad investment base of government bond /agency debt investors, who would not normally engage in infrastructure financing. This broad investment base would enable policymakers to significantly increase the funding targets, unleashing the full potential of markets based financing for the funding of the real economy.

The additional contribution and commitments from national investment banks – on top of the EFSI guarantees by European funds and dedicated to national projects only – could be better integrated within the structure to further increase the leverage capacity with private investors.

EFSI is currently planned to be funded directly by the Commission and the EIB for a perspective amount of €21 billion to be built on in the next 5 years. Clarifications will soon be needed on the constraints and applicability of available resources on the medium-term. To further anticipate future programmes and channels, an informal 'private sector' (open to chambers and associations) steering group could help bring forward proposals.