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Audit brief

The European Fund for Strategic Investments (EFSI)

October 2017

The European Court of Auditors is currently examining whether the European Fund for Strategic Investments (EFSI) is on-track to reach its policy objective of supporting additional investment in Europe.

The Investment Plan for Europe (IPE), the first major initiative of the Juncker Commission, was announced in November 2014. In 2015 the European Fund for Strategic Investments (EFSI), the core pillar of the IPE, was set up jointly by the European Commission and the EIB Group (the European Investment Bank and the European Investment Fund) with the aim of mobilising up to 315 billion euro of additional investments between 2015 and 2018 and to increase access to finance for SMEs and mid-cap companies. This target is to be reached with around 60 billion euro of additional financing from the EIB and the EIF, based on a 16 billion euro guarantee from the EU budget, complemented by a 5 billion euro allocation from the EIB's own resources.

The audit aims to assess whether EFSI is effective in addressing the need to support investment in the EU. In particular, we will examine whether Commission decision-making was based on a clear rationale and sound evidence when designing the support provided under EFSI and the role of national promotional banks and institutions in allocating the financial support from the EIB Group. Our audit also seeks to assess the additionality and added value of EFSI operations.

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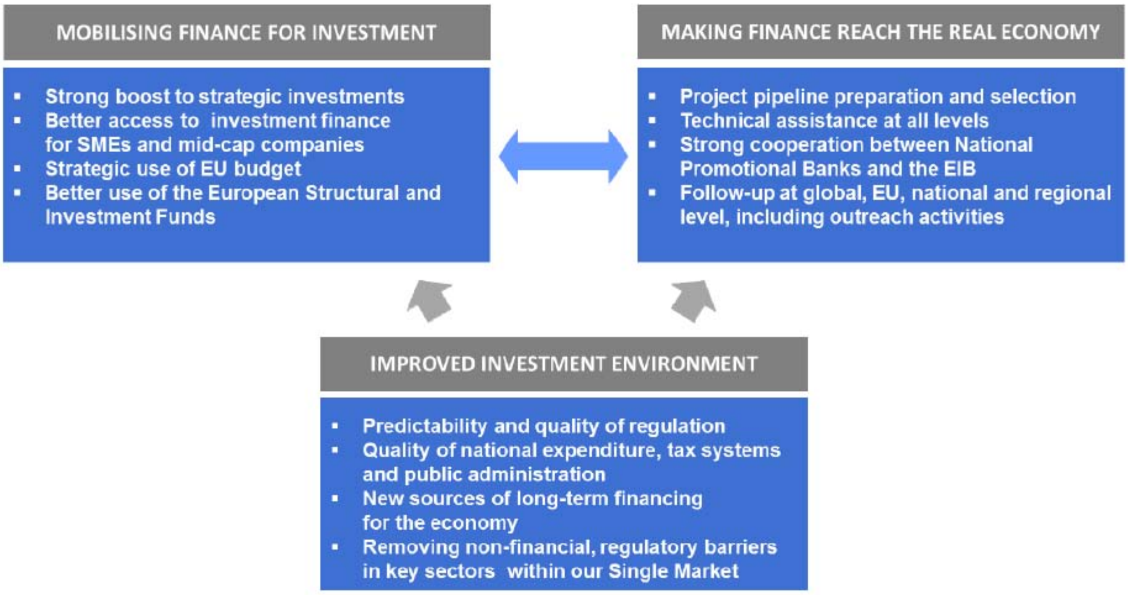
The Investment Plan for Europe (IPE), which is also referred to as the "Juncker Plan", addresses three inter-connected aspects that have an impact on the level of capital investment in the EU economy (see ***Figure 1***). The Plan was announced by the European Commission in November 2014[1].

Figure 1 – An Investment Plan for Europe



Source: COM(2014)903 final of 26 November 2014.

The European Fund for Strategic Investments (EFSI)

The European Fund for Strategic Investments (EFSI) is the first pillar of the IPE and was launched jointly by the Commission and the European Investment Bank (EIB) in July 2015. The purpose of EFSI is "*[…] to support, in the Union, through the supply of risk-bearing capacity to the EIB […] investments; [and] increased access to financing for entities having up to 3 000 employees, with a particular focus on SMEs and small mid-caps companies*"[2].

EFSI was set-up with the aim of mobilising 315 billion euro in new investments in infrastructure, education, research and innovation, and the financing of small businesses over an initial period of three years (2015 to 2018). This new instrument should "*[…] complement and be additional to ongoing EU programmes and traditional EIB activities*" and contribute to "*[…] achieving Union policy objectives such as those set out*" in the COSME Regulation, H2020 Regulation and CEF Regulation[3].

On 14 September 2016, the Commission made a proposal to amend Regulation (EU) 2015/1017[4] establishing EFSI. The Commission proposed extending the investment period of EFSI to 31 December 2020, raising the target for investments to at least 500 billion euro, increasing the EIB contribution by 2.5 billion to 7.5 billion euro, increasing the EU guarantee to 26 billion euro, adjusting the target rate of the related guarantee fund to 35 %, and transferring funds from elsewhere in the EU budget to the guarantee fund. This proposal is currently being discussed in the trilogue negotiations between the Commission, European Parliament and Council. The ECA published an opinion regarding this proposal in November 2016, in which we pointed out that the Commission did not carry out an impact assessment or an *ex ante* evaluation at the time of launching the EFSI in 2015 [5].

EFSI financial and organisational structure

EFSI is not a legal entity separate from the EIB but is set up as a "*[…] distinct, clearly identifiable and transparent facility […] the operations of which are clearly distinguished from other operations of the EIB*"[6]. It has a distinct governance structure, comprising a Steering Board (SB), an Investment Committee (IC) and Managing and Deputy Managing Directors (MD and DMD).

Under EFSI, the EIB provides finance that takes the form of loans, guarantees or equity investments and therefore resembles financial instruments (see ***Box 1***). From a legal point of view, however, EFSI is not a financial instrument under Title VIII of the Financial

Regulation, since it was established under EU law but outside the framework of the Financial Regulation.

Box 1: Definition of financial instruments in the EU's Financial Regulation[7]

Financial instruments are measures of financial support provided on a complementary basis from the budget in order to address one or more specific policy objectives of the Union. Such instruments may take the form of equity or quasi-equity investments, of loans or guarantees, or of other risk-sharing instruments, and may, where appropriate, be combined with grants.

EFSI offers protection to the EIB against potential losses from underlying operations. It is composed of an EU budget guarantee ("the EU guarantee") of 16 billion euro complemented by an allocation of 5 billion euro of the EIB's own capital. The EU guarantee is irrevocable, unconditional and on demand and is backed by a Guarantee Fund ("the EFSI Guarantee Fund"), which has been financed from the EU budget from 2016 onwards and will gradually reach 8 billion euro by 2022 (50 % provisioning rate).

KEY ASPECTS OF EFSI

Eligibility criteria and additionality

In order to be eligible, EFSI projects need to demonstrate that they are economically and technically viable, consistent with EU policies, support any of the general objectives set in Article 9 of the EFSI Regulation, provide additionality, and maximise, where possible, the mobilisation of private sector capital[8].

Additionality[9] is a key feature of EFSI operations and one of the eligibility criteria. EFSI operations should ensure additionality by addressing market failures or sub-optimal investment situations, which could not have been carried out in full (or would have been carried out later) by the EIB, the EIF or under existing EU financial instruments without

EFSI support. EFSI typically targets projects with a higher risk profile than projects supported by normal EIB operations.

The EFSI Regulation also specifies that projects "*[…] shall be considered to provide additionality if they carry a risk corresponding to EIB special activities*" as defined in Article 16 of the EIB Statute and the EIB's Credit Risk Policy Guidelines (CRPG). The EIB therefore considers its special activities supported by EFSI as being *de facto* additional[10].

The EIB, in its 2016 evaluation report, notes that "*[…] there might be situations in which the risk profile does not reflect additionality*"[11]. Also, an independent evaluation of EFSI in 2016 found that in some cases "*[…] special activities are not perceived by the market as having higher risk compared to what the commercial market can offer. Some of the projects could have been financed without EFSI support, albeit possibly at different conditions*"[12].

Added value of EFSI operations

The added value of EFSI operations is defined in the EFSI Investment Guidelines as being their "*[…] contribution to the EFSI objectives*"[13] and encompasses the projects' respect of the eligibility criteria set out in Article 6, including the additionality criteria, and their contribution to the general objectives set out in Article 9 of the EFSI regulation.

The added value of EFSI operations under the Infrastructure and Innovation Window (IIW) is assessed through the EFSI Scoreboard[14], which is based on four pillars:

- the project's contribution to EFSI policy objectives;
- the quality and soundness of the project; and
- the technical and financial contribution of the EIB to the project.

The forth pillar comprises a number of complementary indicators on the project which are specific to EFSI. The IC uses the EFSI Scoreboard to assess the use of EU guarantees for operations.

Mobilised investment and multiplier effect

The most important Key Performance Indicator (KPI) defined in the EFSI Agreement is the one measuring the investment mobilised, for which a target of 315 billion euro was set over the three years following the entry into force of the EFSI Regulation. This target is to be delivered on the basis of a total contribution by the EU and the EIB of 21 billion euro, which results in a target multiplier effect of 15.

The extent to which EFSI mobilises additional funds is calculated on the basis of the 'EFSI Multiplier Methodology'. The central element of the EFSI Multiplier Methodology is the Project Investment Cost (PIC). For investment loans and direct equity investments, the PIC corresponds broadly to the total project cost defined in the EIB loan agreement.

The total eligible investment mobilised, as reported by the EIB at year end 2016 amounted to 126.6 billion euro for signed operations, and for approved operations it amounted to 164 billion euro, which resulted in a multiplier of around 15.[15] as calculated by the EIB[16].

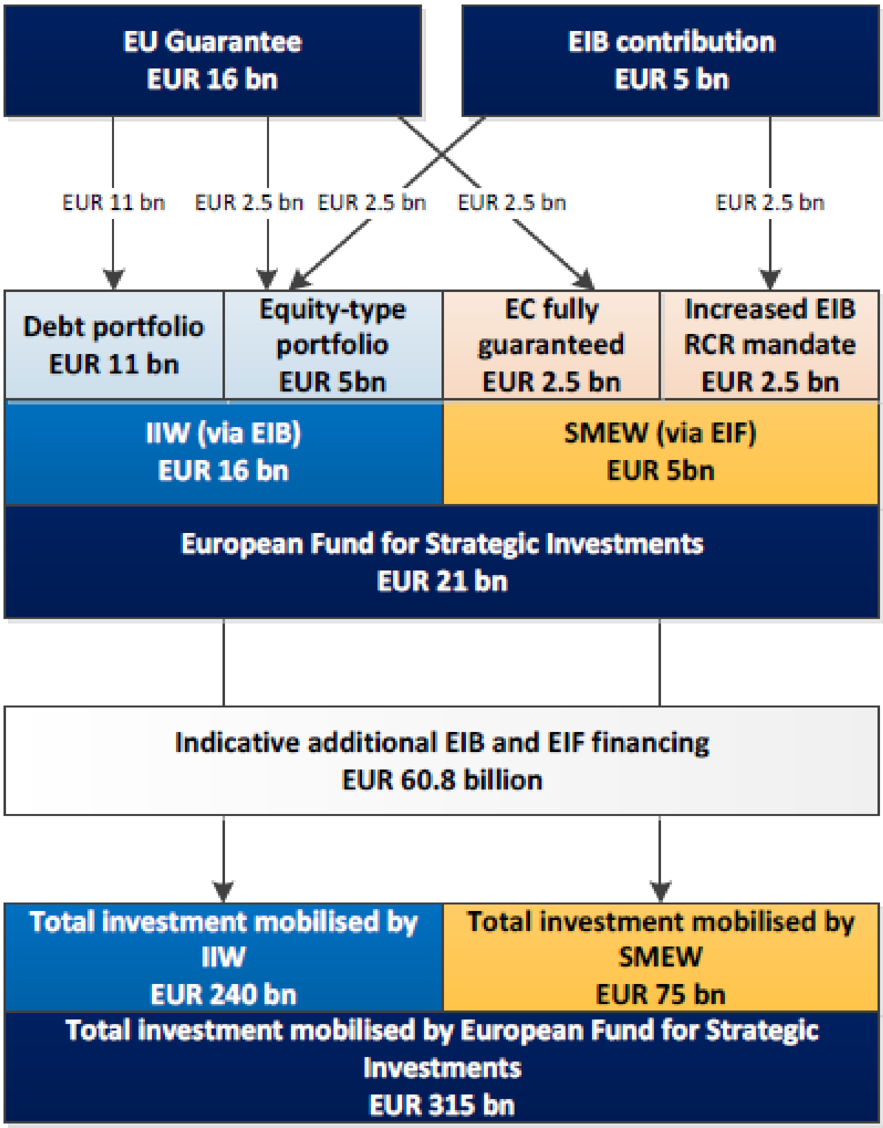
EFSI PORTFOLIO

EFSI's lending and equity investment operations take place within two "windows":

- the Infrastructure and Innovation Window (IIW), managed by the EIB, which aims to provide financing to strategic projects; and
- the SME Window (SMEW), managed by the EIF, which aims to support SMEs.

Each of the windows has debt-type operations, such as standard loans, guarantees and counter guarantees, and equity-type operations, such as direct and indirect equity and quasi-equity participations and subordinated loans (see ***Figure 2*** below).

Figure 2 - EFSI's financial structure



Source: EIB evaluation, 2016.

Under the IIW, the use of the EU Guarantee was initially limited to 13.5 billion euro and 2.5 billion euro from the EIB's own resources for investments in equity operations on equal terms and at its own risk. So far the SMEW debt portfolio has had a significantly higher uptake than the IIW. In July 2016, the EFSI SB reallocated 500 million euro from IIW[17] to increase the SMEW limit to 3 billion euro.

To reach the 315 billon euro target, the EIB Group should provide around 60 billion euro worth of additional financing in three years. The total volume of new Special Activities signatures (including own risk, risk sharing under EFSI and existing instruments like InnovFin and CEF) is planned to increase from around 6 billion euro in 2015 to 17-24 billion euro per annum in the next three years[18].

By the end of 2016, financing for signed EFSI operations amounted to around 20.2 billion euro under the IIW and the SMEW. Moreover, the aggregated investment mobilised was estimated at about 126.6 billion euro (see in ***Table 1***). This corresponds to 40 % of the initial target.

Table 1 – EFSI Investments – as of 31 December 2016 (in million euro)

	Allocated max EU Guarantee	No of operations signed	EIB/EIF signed financing	Total expected eligible investments mobilised related to EFSI signatures	Total expected investments mobilised related to EFSI approvals
Infrastructure and Innovation Window (IIW)	13 000	121	14 169	67 728	94 635
SME window (SMEW)	3 000	225	7 101	58 870	69 509
TOTAL EFSI	16 000	346	21 270	126 598	164 144

Source: EFSI IIW-SMEW Year End Operational Report at reporting date 31 December 2016.

ROLE OF NATIONAL PROMOTIONAL BANKS AND INSTITUTIONS AND INVESTMENT PLATFORMS

The EFSI regulation defines National Promotional Banks (NPBs) and National Promotional Institutions (NPIs) as *"[…] legal entities carrying out financial activities on a professional basis which are given a mandate by a Member State […] to carry out development or promotional activities*"[19].

Initially, several Member States announced their contribution to EFSI, for a total amount of around 42 billion euro[20], the majority of it to be made through the NPBs/NPIs. The NPBs/NPIs can contribute to EFSI by participating in Investment Platforms and/or as co-financiers at the level of individual EFSI-financed projects. By the end of 2016, there were 20 operations (including eight Investment Platforms) signed under the IIW which involved NPBs/NPIs and 73 operations under the SMEW (including the RCR). These operations represented 22.8 % of the signed EFSI finance[21].

Investment Platforms (IPs)[22] are a means of aggregating investment in a set of projects, reducing transaction and information costs and providing for more efficient risk allocation between various investors. The rules applicable to such operations were approved by the EFSI Steering Board in February 2016[23]. As of September 2017, there are 30 IPs approved under the IIW, including three pre-approvals, and three IPs approved under the SMEW.

MAIN RISKS IDENTIFIED WHEN PREPARING THE AUDIT

When preparing our audits we carry out a risk analysis of the policy area or programmes that we intend to examine. For our audit on EFSI we identified risks related to the following areas:

- additionality of EFSI to traditional EIB activities;
- coherence and complementarity of EFSI with traditional funding instruments under the EU budget;
- the measurement and reporting of the public and private investment mobilised; and
- the involvement of National Promotional Banks and National Promotional Institutions and the promotion of investment platforms in the Member States.

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Our special reports set out the results of audits of EU policies and programmes or management topics related to specific budgetary areas.

Audit briefs provide background information based on preparatory work undertaken before the start of an on-going audit task. They are intended as a source of information for those interested in the audited policy and/or programme.

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1 COM(2014) 903 final of 26 November 2014.

2 EU Regulation 1017/2015 of 25 June 2015 (EFSI Regulation), Article 3.

3 EFSI Regulation, Recitals 8 and 13.

4 COM(2016) 597 final of 14 September 2016.

5 ECA's Opinion No 2/2016 concerning the proposal for a Regulation of the European Parliament and of the Council amending Regulations (EU) Nos 1316/2013 and 2015/1017 and the accompanying Commission evaluation in accordance with Article 18(2) of Regulation (EU) 2015/1017

6 EFSI Regulation; Article 4.

7 EU Regulation 966/2012 (Financial Regulation), in Article 2(p); identical definition in EU Regulation 1303/2013 (CPR), Article 2(11).

8 EFSI Regulation, Article 6.

9 EFSI Regulation, Article 5.

10 Evaluation of the functioning of the European Fund for Strategic Investments (EFSI), Operations Evaluation, EIB, September 2016, p. 23.

11 Idem, pgs. 15, 16.

12 Ernst & Young, "Ad-hoc audit of the application of the Regulation 2015/1017", 14 November 2016, page 3.

13 EFSI Regulation, Annex II, point 4.

14 Commission Delegated Regulation (EU) 2015/1558 of 22 July 2015, Article 1.

15 European Fund for Strategic Investments, 2016 End-Year Operational Report

16 The Commission reports, in September 2017, that the total of 236 billion euro in expected investments were mobilized

17 Revised EFSI Agreement, Article 7(3).

18 The EIB Group Operational Plan 2016-2018

19 EFSI Regulation, Article 2(3).

20 http://europa.eu/rapid/press-release_IP-15-5420_en.htm.

21 European Fund for Strategic Investments, 2016 End-Year Operational Report]

22 EFSI Regulation, Recital 34.

23 http://www.eib.org/attachments/general/efsi_rules_applicable_to_operations.pdf.