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"THE JUNCKER PLAN"

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Keynote Speech

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The Juncker Plan must not be considered just as a new large Guarantee Facility for European SMEs, corporates and infrastructure. It is first of all a major anti-cyclical tool to boost investment, growth, jobs creation and competitiveness.

The Plan – however – should also be thought as a first step towards the creation of a Single European Market for Infrastructure, SMEs Financing, and Corporate Financing.
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With an aging population, a public debt overhang, and the tough competitive challenge coming from emerging economies, the EU should rely on a system for financing infrastructure and SMEs which weighs as little as possible on public finance. The new model should be technically very advanced, as well as financially reliable, in order to attract long term investors and private capital around the globe, where liquidity is great but is directed where risk is lower and yield is higher, and where the demand (and the competition) for capital investment will increase, at exceptionally high rates, throughout the XXI Century.

The fall of investment in the EU – equal to -20% since 2008 (BCE, September 2014) – has been one of the main factors of the long recession which has hit EU economies; it is responsible for a sharp decrease in the competitiveness of European firms at the global level.

The European Member States, following the requirements of the Fiscal Compact, have achieved significant results in the process of fiscal consolidation. Fiscal responsibility and financial stability are conditions for growth and competitiveness, but alone are not enough for a full economic and fiscal recovery. A strong investment boost, especially in innovation, R&D, technology, infrastructure and education is equally needed.

The time then is right for an infrastructure investment push. The IMF, in its *World Economic Outlook* (11 September 2014) maintains that better and more public infrastructure investment is critical. The impact of such investment is stronger when there is economic slack, and when investment efficiency is high. If done correctly, the boost to output offsets the debt taken.

It is well known, in fact, in economic theory, that investment is crucial to spark growth and to enhance competitiveness, as well as to eliminate imbalances. Particularly, investments in infrastructure, innovation, R&D, technology and human capital have a significant positive effect on potential GDP growth. The debate in the scientific literature concerns only the measurement and size of this effect.

According to IMF last findings (September 2014), increased public infrastructure investment raises output in the short term by boosting demand and in the long term by raising the economy's productive capacity. In a sample of advanced economies, an increase of 1 percentage point of GDP in investment spending raises the level of output by about 0.4 percent in the same year and by 1.5 percent four years after the increase. In addition, the boost to GDP a country gets from increasing public infrastructure investment offsets the rise in debt, so that the public debt-to-GDP ratio decreases. In other words, public infrastructure investment could pay for itself if done correctly.

The success of the Juncker Plan depends largely on the fulfilment of certain conditions or prerequisites. The Plan requires, first of all, the approval and implementation of a number of national and European structural reforms needed to create the proper institutional and market framework for infrastructure and firms investment: liberalizations, legislative stability, streamlined and fast administrative procedures, light regulatory burdens, fast and reliable judicial systems, efficient and technically prepared public administration, information platforms, transparency, technical assistance, cutting red tape, etc. The capacity to attract investments from global markets is strongly dependent from the successful implementation of these long-waited reforms.

The sectors involved in the Plan are broad: strategic infrastructure in transport, energy and broad-band, social and urban infrastructure, R&D and innovation, education and heritage, support to SMEs and corporates. Eligible counterpart are also broader than at first expected:

corporate of all sizes; utilities; public sector entities; SMEs and Mid-Caps; National Promotional Banks (NBPs) or commercial banks for intermediation; dedicated platforms.

The risks taken by the operations of the Plan will range from equity, mezzanine, and subordinated debt to senior loans. Operation supported by the EFSI guarantee will typically have a different risk profile than normal EIB operations. However, the process of risk assessment (including probability of default and recovery rate calculations) should follow EIB standard criteria and will quantify the total risk absorption of each operation on which the guarantee will be measured to provide the enhancement required, without putting at risk EIB balance sheet, but, at the same time, making eligible projects and operations which at market standards alone would not had been bankable.

For equity type of operations, EIB shall provide either direct financing to individual companies or projects, or financing for equity funds or analogous risks. Equity investments should be priced according to a "fair rate of return" and debt product with EIB's normal practices.

"Additionality" is the guiding concept of the Plan. The principle is needed for the support by the EFSI of operations which address market failures and sub-optimal investment situation. The EIB will carry out its standard risk assessment and will quantify the total expected loss for each operation. The computation shall be performed excluding First Loss which will be provided by the EFSI Guarantee. The EIB risk assessment will be classified according to the risk underlying the operation by the EFSI and the guarantee provided according to the credit enhancement required to make the operation financially sustainable. The level of the credit enhancement will be generally higher than the equivalent limit normally given by EIB. The limit maybe amended by time to time.

Following the additionality principle, Juncker guarantees, if needed to face market failures and if granted with competitive procedures, should be always considered compliant with State Aid rules. The goal is in fact to help in leveling the playing field at the global level, in order to allow European SMEs, PFI and PPP projects to compete in the global market. The European State Aid discipline has been originally designed to favor fair competition by levelling the playing field in the single market; the fair competition should have ensured efficiency, innovation, growth and a healthy "creative destruction". Consequently, to forbid State Aid granted to reduce competitive handicaps contradicts the original rationale on which State Aid discipline was first introduced. However, in the new global scenario, the same rationale should now apply also to EU interventions, which aim is to reduce the competitive handicap that European firms still have.

The pricing of the guarantee should be coherent with the objectives of the Investment Plan, to allow for the financing also of non-investment grade projects, whose rating is due to intrinsic complexity such as macro-financial constraints (e.g. national ratings). A cost at full market price would not be appropriate to address market failures and gaps, and to stimulate additional investment. I suggest to price the Juncker guarantee in line with previous EU Financial Instrument like the European Energy Efficiency Fund.

Another important pillar of the Plan is the recognition of the role which can be played by National Promotonal Banks and Institutions (NPBIs). The NPBIs stand ready to give an important contribution to the implementation of the Plan, ensuring "additionality" over existing operations and further enhancing cooperation with the EIB to this end. Their shared objective is to make the most effective use of the available funds to mobilize additional public and private investment. They are ready to expand their activities with the complementary support of the increased EIB risk capacity (part-covered by EFSI), in the following areas:

- Increasing investment activities in ABS Transactions, acting as an anchor investor or providing structuring expertise in the field of securitization,
- providing technical assistance and improving access to funding via Global Loans and guarantees,
- investing in Venture Capital Funds and/or Fund of Funds,
- increasing commitments in Fonds Marguerite, which targets equity and mezzanine investments in projects,
- boosting project finance or public-private partnerships for eligible infrastructure projects,

NPBIs engagement should continue to rely foremost on national requirements and supervision and is already guided by EU regulations. Any further and legitimate EU regulation towards NPBIs and EIB should not hinder their ability to fulfill their specific promotional objectives.

The role of the national, regional and sectorial platforms is crucial. The NPBIs may concur with EIB to finance both single projects and platforms. It would be preferable that the Juncker guarantees be given directly to platforms and not only to contribution of the EIB to the platform.

The Plan requires a sharp and effective decision making process, in order to give an anti-cyclical boost to investment already in the second term of 2015. So, we should take off the ground most of the projects and/or Platforms in 2016. Therefore, an excessive "bureaucratization" in the process of validation must be avoided. The platforms, instead, should have a direct mandate to perform on their own the due diligence of each single

projects and projects' portfolios (in particular, for Platforms focused on SMEs and small/medium infrastructures). These processes may be followed, eventually, by ex-post sample controls by the Investment Committee.

A fast and efficient deployment of the Juncker Plan will be best ensured if the increased EIB Group risk capacity could be coupled with NPBIs existing and well proven products which support the objectives of the Plan. The increased EIB Group risk capacity should be available, as requested by NPBIs and as appropriate, in the form of loans or guarantees. The higher risk capacity should translate into EIB Group supporting also riskier transactions financed jointly with NPBIs. It should be granted access for NPBIs proposing viable projects to all EFSI products, available from the increased EIB Group risk capacity.

To give an anticyclical boost to investment and growth as rapidly as possible, the cooperation between the EIB and the NPBIs could be used to activate some tools capable of delivering timely results, based on the common understanding of the current EFSI draft regulation according to which EIB could grant a guarantee or loan or equity-type to a NPBI or a project proposed by a NPBI under a partial counter-guarantee of the EU Budget.

I cite only a few examples:

- To finance SMEs , NPBIs and the EIB could provide funding and guarantees to intermediary banks, especially in markets with shortfalls in bank lending; the EIB Group could also provide risk sharing capacity or guarantees in support NPBIs' activity.
- EIB and NPBIs could contribute to revitalizing the European securitization market and to establish a stable investor base to support funding, capital relief, reduction of concentration risk, and/ or deconsolidation for originators.
- NPBIs and the EIB Group could engage in investing in and potentially structuring of securitization transactions, which would be strengthened by EIB Group participation in mezzanine and especially junior tranches.
- NPBIs and the EIB Group would be able to invest fast and efficiently in venture capital funds of funds, with partial coverage by EFSI supported guarantees.
- A doubling of the Marguerite Fund' current available resources may be an option already in 2015, by widening its sectorial approach, increasing its brownfield investments, and by making some minor changes in its rules of governance and engagement.
- EIB and NPBIs could enhance the European Energy Efficiency Fund (EEEF) by slightly removing some current investment limitations (i.e. investment types and/or country limits, …) and simplifying eligibility and selection criteria.

Finally, some changes are required in an international and European regulatory framework still un-friendly to long term investment. A re-calibration of actual prudential regulations and accounting standards (IAS/IFRS, CRD IV and Solvency II/Omnibus), is long time due: consensus is now quite general, but no concrete results have been so far achieved. On the contrary, the Basel Committee is debating a new set of rules (Basel IV) which would make

even harder (in terms of capital absorption and liquidity ratios) to finance investment and the real economy. The risk – at the end – is that EIB and NPBs are left alone in a market where other potential investors will have no convenience to participate, even if they wished to do so, due to the effects of rules drafted with no clear understanding that economic growth (that is, long term investment) are a binding condition for both financial stability and long term sustainable fiscal consolidation.

We should not forget that one of the fields on which global competition is playing its game is the setting of prudential regulations and accounting standards. The tough prudential and accounting regulation which penalize the financing of real economy and infrastructures has become a major weapon in the global economic and financial war, which characterize the XXI Century, hitting Europe more than others economies. The EU financial system, which is more bank-oriented than most of other major financial system in the world, pays in fact a greater price due to prudential regulations and accounting standards unfriendly to LTIs and to the financing of the real economy. This is not the case for market-based financial system such as the US and Government based financial systems such as China.

Moreover, the UE Member States have stricter space of manoeuver in the substitution of banking financing with State Aid. Finally, the European political and regulatory Authorities are always much more rigorous in the transposition and implementation of international regulations and generally provide less exemptions and less flexibility than those of other major countries (see for instance the transposition of Basel II and Basel III made in the US).

Ladies and Gentlemen,

After the crisis the US has launched two major Plans for boosting investments. The first plan in 2009, financed mostly on debt, worth around USD 900 billion for investments in infrastructure, education, health, energy, unemployment, benefits and other social welfare spending, and tax incentives. The second plan, announced at the beginning of this year by President Obama, worth almost USD 500 billion to finance public works by an increase of taxes on wealth and corporation. The US can afford it, thanks to: a better demographic perspectives due to well target immigration policies; half of EU welfare costs weighting on public finance (pensions and health); a much higher defense spending (17% vs 1,5% of the EU) with its well-known high-tech Keynesian effects; and the privilege of the dollar due to its role as a super-power. The multiplier effects have been extremely positive on economic growth, employment and competitiveness.

In the present macroeconomic and fiscal conditions, European Member States cannot afford the same policy; cannot increase dramatically investments financed with budget resources. However, the European Union could do it, taking up the proposal by Jacques Delors to issue Eurobonds to finance a plan of strategic investments for Europe. However,

proposals to use Eurobonds to mutualize national sovereign debts have jeopardized Delors-like plans for issuing large amounts of Eurobonds for growth and investment. Maybe in the future the Union will be able to reconsider financing growth by issuing Euro-debt – at least for a partial part of it. But not now.

Europe needs to boost investment as much as the US. In the present conditions the only way to do it is through a smart, rigorous and rapid implementation of the Juncker Plan. All of us must work for its success. Since the success of the Juncker Plan represents a good step towards the success of Europe.