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REFORM BAROMETER

REFORM TO PERFORM - ANNEX I

THE COMMISSION'S INVESTMENT PLAN 1 YEAR ON

2012 2013 2014 2015 2016

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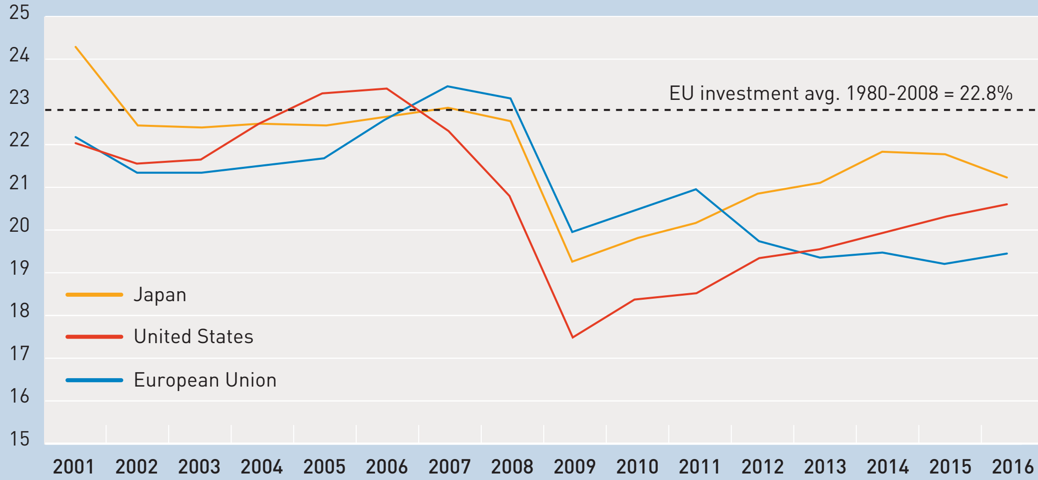
The Commission's Investment Plan 1 year on

EU investment, in common with other major economies, declined significantly following the financial crisis. In particular, investment in the housing market experienced strong declines. But while investment as a share of GDP has rebounded strongly in the US and Japan, EU investment experienced a second dip as the subsequent sovereign debt crisis developed in 2011 and is only starting to bounce back very slowly, while remaining well below its long-term historical average (fig 1).

Figure 1 **US and Japanese investment recovered more rapidly than EU investment after the crisis**

Investment as % of GDP in the US, Japan and EU, 2001-2014



Source: IMF, World Economic Outlook, October 2015

Given investment is the basis for our future competitiveness, growth and jobs we welcome the European Commission's decision to prioritise investment. This box assesses the progress made since the Commission's Investment Plan was launched just over a year ago. We firstly consider progress on the first pillar of the investment plan, the European Fund for Strategic Investment (EFSI), analysing the composition and volume of initial project funded by the plan. Secondly, we consider progress on policy measures to break down barriers to investment which will be key to long-term investment performance. Finally, we consider how these initiatives are impacting on overall investment levels and intentions in the EU.

1. The European Fund for Strategic Investment (EFSI)

A key part of the Commission's investment plan was to launch a new instrument, the European Fund for Strategic Investment (EFSI) aimed at using public funds to leverage private investment, in projects ranging from large infrastructure to SMEs. The EFSI is backed by a €16 bn guarantee from the EU and €5 bn from the European Investment Bank (EIB) from which it is hoped €315 bn of new lending will be generated. 2015 saw the EFSI regulation approved by Member States and voted through the European Parliament. In addition, the Managing Director of the EFSI who also serves as Chair of the Investment Committee, as well as Investment Committee members have now been selected and the Investment Committee formal started its work at the end of January 2016. However, the EIB and EIF (European Investment Fund) were already able to start approving and/or signing projects with the Commission providing sign-off in absence of the investment committee.

According to the EIB's latest figures[6], 145 transactions in 22 of 28 countries were signed off by the EIB andthe European Investment Fund (EIF). This led to total financing by the EIB of €6.7 bn and €2.3 bn by the EIF, resulting in total investment according to the EIB of €61.5 bn.

This lending would represent 19.5% of the €315 bn target, emphasizing that whilst the EFSI has made a good start, the pace of lending, particularly through the EIB side will need to be stepped up if the 3 year target is to be met[7].

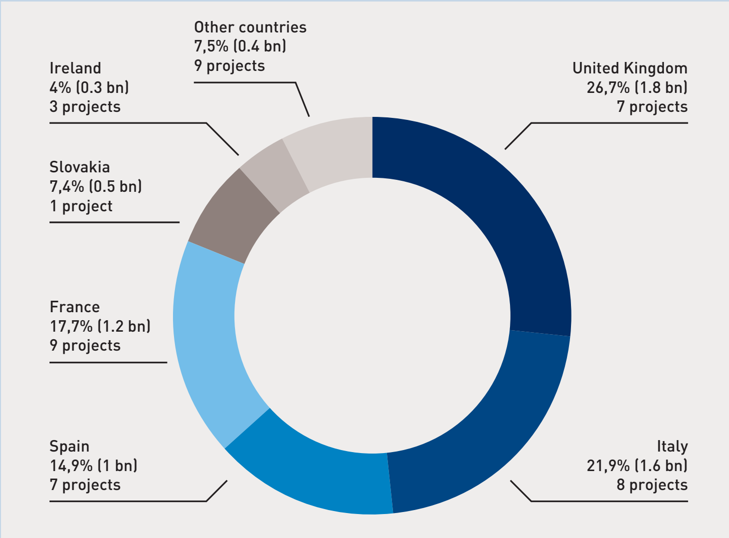
It will also be important that the EIB steps up its efforts both to ensure and demonstrate that lending counting towards the €315 bn target really is additional and not replacing (crowding out) private investment. In particular, for EIF funding, where the leverage ratio is already much higher, it will, for example, be important to ensure that investment in venture capital firms is used to fund small business growth and not simply management buyouts. Where national development banks (NDB) have provided co-funding to EFSI projects, it will be important to check that EFSI contributions have not had an impact on other activity of the NDB.

Regarding **sectoral balance**, the EIB's own assessment shows that a large proportion (39%) of the EIB and EIF projects fall in the area of energy, environment and climate, while 19% of the funds relate to projects in the transport sector and 10% to digital infrastructure. Smaller businesses receive 27% of all EFSI financing.

In terms of **geographical balance** (fig 2), we are able to provide a more detailed analysis of EIB lending under the EFSI to a total of 47 projects, drawing on EIB press releases[8]. The UK has been the largest recipient of funds (27%), followed by Italy (22%). But two further points are also salient. Firstly, with the exception of Slovakia, a number of Member States that joined the EU since 2004, who have traditionally received significant structural funds have so far made limited use of the funds. Secondly, it also appears the case that until now very few cross-border projects have been approved[9].

Figure 2 **EFSI – location of approved projects**

Geographical composition of projects as share of total contribution and number of projects



Source: EIB Press Releases from 15 Nov. 2014 to 15 Jan. 2016

[6] EFSI dashboard (updated 2 February 2016)
[7] Previous figure released at the "EIB press conference on 2015 results" showed that while total financing of €5.7bn by the EIB led to a total investment of €25 bn, the EIF's financing of only €1.8 bn also resulted in total investment of €25 bn.
[8] These cover €6.7bn of lending through the EIB. Although the figure is the same as the one presented by the EIB in its January press conference, any small discrepancy is due to limited data availability.
[9] The exception being the GINKGO FUND II project involving France and Belgium as well as the SAARLB - RE PROJECT FINANCE GUARANTEE involving Germany and France.

2. Breaking down investment barriers in Europe – key policy development

It is clear that the EFSI can only reach its ambitious leverage objectives if the EU also removes barriers to investment, which is the third pillar of the Investment Plan. Initiatives in 4 keys area are analysed in more depth in table 1.

Overall we see that the Commission has set out a number of ambitious strategies that, if fully implemented, alongside broader initiatives to reduce and improve the quality of regulation in the EU, would be a significant step towards making Europe a more attractive place for businesses to invest.

However, in many respects, the hard work starts now, with Member States and Parliament needing to work constructively together to rapidly implement the ideas set out in the action plan and help improve the investment environment in the EU.

Table 1: Overcoming barriers to investment

	Commission Action	BUSINESSEUROPE Action
SINGLE DIGITAL MARKET	The Commission published a Digital Single Market Strategy in May 2015. The strategy aims to make Europe a leader in the global digital economy and create a Digital Single Market, where the free movement of goods, persons, services and capital is guaranteed and where citizens and businesses can seamlessly access online goods and services throughout Europe. Key initiatives include: ▪ Legislative proposals for: a **reform** of the **copyright regime**; to reform the current **telecoms rules**; on **contract rules for tangible goods and digital content**; ▪ Actions to **tackle unjustified geo-blocking**; ▪ **Analysis of the role of platforms in the market including illegal content on the Internet**; ▪ **Initiatives on data ownership, free flow of data and on a European Cloud.**	The Digital Single Market Strategy is a first step in the right direction. The Commission identified the right areas where action is needed to boost the European digital economy, particularly through competitiveness-oriented initiatives such as the digitalisation of industry roadmap. Any legislative approach in this field must follow the principles of simplification and technology-neutrality; ensure the level-playing field amongst players offering the same services and avoid creating unnecessary rules. Positive initiatives include: ▪ Efforts to **improve the free flow of data** as addressing unjustified restrictions to the free movement of data is crucial for the development of the digital economy. ▪ **Reform of the current telecom rules** - networks are the foundation of the digital economy. The Commission must promote investment in innovative infrastructure. Initiatives to reduce unjustified **geo-blocking** and to address the issue of platforms, while welcome, need to be taken forward carefully.

ENERGY UNION AND CLIMATE

Commission Action

Energy prices have a strong impact on businesses, particularly in manufacturing industry. Technical or regulatory barriers hold back energy providers to freely compete.

The Commission strategy on implementing the Energy Union, published on 25 February 2015 focuses both on undergoing transforming the electricity system to integrate and regulate national energy markets, and well as on investing in new projects to improve the security and diversity of energy supply in the coming years. In addition the strategy emphasizes the need to take full advantage of the EU's renewable energy potential.

This strategy includes measures such as:

- Legislative action to revise the **EU ETS, effort sharing, renewable and energy efficiency** directives.
- **195 key infrastructure projects** to implement the Energy Union were selected to reach the goal of an energy interconnected Europe in the framework of the Connecting Europe Facility.
- Revision of regulations on **intergovernmental agreements** and **on security of gas supply.**
- Proposal for **regulation on the redesign of the European electricity market.**

In addition, we have seen the conclusion of an ambitious and legally-binding agreement on **COP21 in Paris** in December 2015.

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Progress has been made on energy security and on energy markets. The forthcoming power market design proposal must aim to attract investment, and to ensure that existing capacity mechanisms are not distortive.

In addition, more progress is needed on the development of key energy infrastructures and interconnection projects in order to allow energy to flow freely in response to market needs and to eliminate energy islands and bottlenecks.

The COP21 agreement is a major step forward in fighting the impacts of climate change, although it does not solve the major issue of competitiveness between countries. Countries must now fully deliver on their commitments.

Regrettably, the proposal on the post-2020 EU ETS reform, by reducing drastically the volume of free allowances, fails to support the competitiveness even for the most efficient industries.

On the revision of intergovernmental agreements on gas supply, it remains unclear to us how serious the problem is, and to what extent competition will be hindered and security of supply is undermined.

CAPITAL MARKETS UNION

Commission Action

The Commission adopted on 30th September 2015 an Action Plan setting out the measures to achieve a single market for capital in Europe. By reducing the barriers to capitals flow in the EU, the Capital Markets Union will create new opportunities for both savers and investors.

The Commission plans to revise the regulation and structure of financial systems to reduce the cost of financing for firms and enlarge the base of potential investors for new projects. This renovated regulatory framework will also strengthen and stabilize the financial sector.

These measures include:

- An initiative to **boost EU securitization market.**
- Consultations on **venture capitals and social entrepreneurship funds, on covered bonds, and on an EU regulatory framework for financial services.**
- Amendments to the **Solvency II regulation** to recalibrate capital requirements to encourage long-term investment, particularly in infrastructure.
- Proposals to streamline **prospectus requirements** for firms accessing capital markets.
- Decision to undertake a **cumulative impact assessment of financial regulation**.

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The Commission's proposal on the Capital Markets Union is an important initiative to try and improve the use of capital markets and broader equity markets in the EU.

We have been particularly encouraged by proposals described on the left around securitization, encouraging long-term investment and assessing the cumulative impact assessment of recent regulatory reform in the financial sector (long overdue).

However, there remains a lot of work to do in terms of the Commission and Member States, implementing the many changes, often quite technical, that are required to help develop EU capital markets.

Following the publication of the comprehensive impact assessment on financial regulation, the European Commision should consider whether further action is required to ensure prudential rules strike the right balance between increasing financial stability and supporting companies' financing needs for investment and business activites.

TRADE AND INVESTMENT AGREEMENTS

Commission Action

The Commission has recently come up with its new Trade and Investment Strategy on 14 October 2015. The strategy emphasises the need to make trade policy more inclusive, more transparent and to promote EU standards.

The EU trade agenda includes a number of bilateral trade and investment negotiations with some of our key trading partners, these include:

- The **Transatlantic Trade and Investment Partnership (TTIP)** aims to be the most ambitious trade and investment agreement ever negotiated by the EU. The agreement should reduce the costs of trading and investing in the transatlantic market and create new opportunities for companies on both sides of the Atlantic, especially SMEs.
- The EU is also negotiating an ambitious trade and investment agreement with **Japan**. The main objective is to address non-tariff measures that constitute a real obstacle for EU products to access the Japanese market.
- The EU and **China** are negotiating a Bilateral Investment Agreement aimed at improving market access as well as setting high standards for investment protection.
- The Commission has also made a new proposal to replace the Investor to State Dispute Settlement Mechanism (ISDS) in all the agreements being negotiated by the EU that include investment protection.

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In order to improve confidence and boost investment EU companies need to have more and better business opportunities in third markets. The Commission's new Trade and Investment strategy sets ambitious goals.

Trade policy can lead to political and economic stability, increased sustainability or more transparency but only if the EU manages to successfully negotiate and implement ambitious agreements that translate into better and wider market access for companies. Therefore it is crucial to speed up the process of adoption and implementation of concluded agreements like with Canada and Singapore.

Concluding the agreement with the US is critical to foster trade and promote new investment both in and outside Europe. In 2016 the EU and the US must make substantial progress in the negotiations leading to a political agreement during the Obama Administration.

Similarly for Japan and China, the EU should be able to negotiate ambitious agreements that open new trade and investment opportunities for our companies by addressing Non-Tariff Measures and existing limitations to FDI.

The new Investment Court System (ICS) proposal introduces significant changes in the procedural aspects but also in the level of protection granted to investors. These changes can significantly hamper the possibility for EU investors to uphold their legitimate rights, negatively impacting investment.

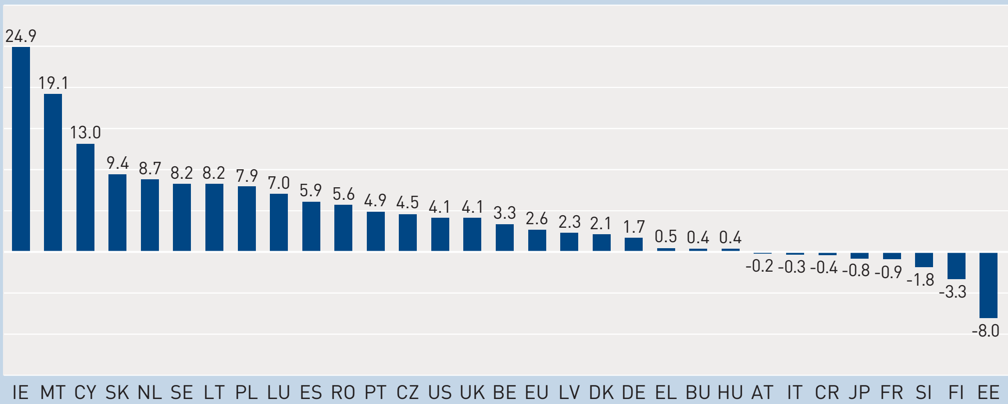
3. Results – are investment intentions improving in Europe?

Assessing the impact of the Commission's plan on overall investment in the EU is clearly difficult given both the significant time delays between policy changes been made, investment decisions being taken and investment actually taking places, and the range of political, financial and external factors that can impact on investment.

Official data suggests overall in the EU there has been only a very moderate increase in investment over the last year. Specifically in the 12 months from October 2014 to September 2015, provisional data shows EU investment grew by 2.6% compared to the previous 12 months (fig 3). This contrasts with investment growth during same period in the US of 4.1%. But within the EU, there are significant variations, with strong investment growth in the last year particularly in countries that have undertaken economic reform including Ireland (24.9%), Cyprus (13.0%) and Spain (5.9%).

Figure 3 **While we see strong variations, EU investment growth over the last year lacks that of the US**

Total investment in Q4 2014 to Q3 2015 compared to the same period in the preceding year, % change

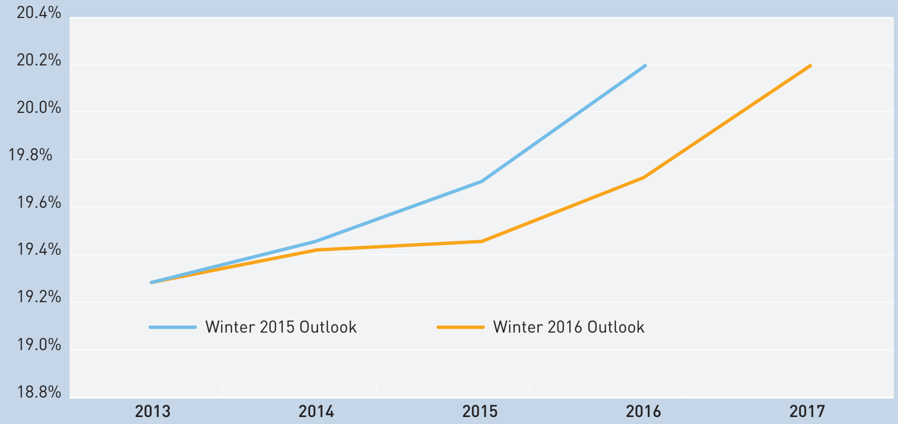


Source: Eurostat, Bloomberg Terminal, FRED

The fact that that **investment intentions do not seem to be picking up** adds to concerns about investment prospects. The Commission's Autumn 2015 forecast for investment, which draws on an EU survey of businesses' investment intentions shows a much slower pick-up in investment in the coming years than had been expected 12 months previously (fig 4).

Figure 4 **Commission's investment forecast revised downwards over the last 12 months**

Change in investment expectation as share of GDP, EC Winter 2015 & 2016 Economic Outlook



Sources: Commission Economic Outlook, BUSINESSEUROPE calculation

Conclusions

The last 12 months have seen investment in the EU fail to pick up as strongly as expected, with the Commission now forecasting lower investment levels in the coming years than it was doing 12 months ago. But this shift should not be seen as a failure of the Commission's investment plan. Business investment has clearly been impacted by the inter-related factors of rising geo-political tensions both inside and outside the EU, slowing emerging market growth and increasing financial market instability.

Policy-makers have made important steps forward in quickly establishing the EFSI and ensuring it can start lending. Meeting the € 315 bn target will be particularly challenging given increased geo-political tensions that have the potential to increase uncertainty around the profitability of many potential projects. The EFSI investment committee must also focus on supporting financially sound projects that cannot find private funding alone and resist any pressure to fund projects unnecessarily, and crowd out private lending, simply to meet the € 315 bn target.

Important steps have also been made by the Commission in setting out the policy barriers that need to be addressed in many important areas such as trade, capital markets, energy and the digital economy, if EU investment is to increase. Policy-makers now need to urgently implement many of the ideas set out in strategy papers and start taking concrete steps to improve Europe's business environment.

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BUSINESSEUROPE is the leading advocate for growth and competitiveness at European level, standing up for companies across the continent and campaigning on the issues that most influence their performance. A recognised social partner, we speak for all-sized enterprises in 34 European countries whose national business federations are our direct members.

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