Andrew McDowell

Vice-President, European Investment Bank

A pan-European response to a disease that knows no borders

Even as the spread of Covid-19 slows, and discussions commence on how to ease the economic shutdown, otherwise healthy European businesses are still failing by the thousands, suffocating from a lack of revenues and financing.

This pan-European pandemic calls for a pan-European economic response.

This is why EU Finance Ministers have endorsed the European Investment Bank (EIB) proposal for EU Member States to create a €25 billion Guarantee Fund to enable the EIB Group to mobilise up to EUR 200 billion in funding for distressed sectors, as part of the wider EUR 520 billion package of EU crisis response measures agreed on April 9.

How the guarantee fund would work

The €25 billion guarantee fund will – subject to national confirmation and approval processes – be financed by EU Member States pro-rata to their shareholding in the EIB and/or other institutions. It is limited to addressing the Covid-19 shock, but could form a bridge between the crisis and the recovery periods.

With the benefit of a counter-guarantee from the Fund, the EIB Group – the Bank and the European Investment Fund (our specialist SME guarantee and equity subsidiary) – will unlock financing to the real economy by ramping up guarantees to local lenders, national promotional institutions and other financial intermediaries.

The products to be rolled out under the Guarantee Fund will likely be dominated by capped (first loss) and uncapped guarantees on portfolios of SME loans originated by local lenders and other forms of risk-sharing on new and existing corporate loan portolios. Some of these will provide regulatory capital relief.

Other products will also be considered, including participations in Asset Backed Securitisations to free up lending capacity, as well as equity investments in venture capital and private equity funds supporting innovative firms.

This fund should also allow EIB to counter-guarantee some national guarantee schemes already in place, thus sharing across the EU the risk of these schemes and increasing their firepower.

The focus will be on SMEs, though it is proposed that mid-caps and larger corporates will also be eligible for support. All must be viable in the long-run and, in the absence of the Covid-19 pandemic, would meet commercial requirements for financing.

EIB and EIF have years of experience in these products, and through existing network of hundreds of counterparts can quickly channel financing to markets and sectors most in need. While there will be no quotas for any country, we have proposed upper concentration limits to ensure an equitable allocation of the firepower, always guided by EIB's usual assessment of economic and social impact.

A pan-European response to the pandemic

I see four key advantages of supplementing – at the EU level – the many national guarantee schemes that have already been rolled out.

Firstly, as with the Covid-19 health crisis, we need a co-ordinated approach to managing the economic crisis. No country will recover alone. Even the largest is influenced by what happens in terms of overall EU demand, intra-EU trade, intra-EU value chains, overall EU market confidence and financial market loops.

A study by the European Central Bank shows that 1% symmetric decline in the GDP of each Member State brings, after the initial mechanical effect, an additional 0.6-0.8% decline in the Euro-area GDP growth, due to the direct and indirect spillovers in trade. The EIB's own data shows that 40% of economic growth and growth in jobs from the operations we finance comes from cross-border spill-overs.

Secondly, by pooling credit risk across all of the European Union, the overall average cost of the fund could be reduced, compared to national schemes.

Thirdly, the use of the EIB also means that guarantee schemes – and their SME and corporate beneficiaries – across the EU could benefit from the the bank's AAA rating, even in financially weaker Member States which lack fiscal space and a top credit rating. With the suspension until December 2020 of normal state aid restrictions, this can help to level the playing field for businesses across EU countries during both the crisis and recovery period.

Finally, Europe's venture capital and innovation ecosystems are trans-national by nature – no individual Member State has adequate incentives to fully protect them, calling for a pan-European perspective and policy instrument.

The broad product mix being proposed will ensure that in every country we will find a way to complement national schemes to best effect.

The economic and financial dynamics immediately ahead of us are approaching a tipping point: we have little time to put in place measures to safeguard the European economy from this unprecedented shock. By responding to this crisis with a spirit of solidarity and enlightened self-interest, we can start to strengthen confidence among markets and citizens in Europe's capacity to weather the storm. Together, Europe can emerge from this crisis even stronger. ●