

EUROPEAN INVESTMENT BANK

CA/215/87
15 June 1987

DRAFT

PV/87/10

B O A R D O F D I R E C T O R S

Minutes of meeting held in Luxembourg on 12 May 1987

12. ADDITIONAL MEANS FOR PROVIDING GUARANTEES FOR EIB LENDING WITHIN THE COMMUNITY (Doc. 87/208)

The CHAIRMAN, introducing Document 87/208, remarked that the subject was one which the Management Committee had been thinking about for some time, and which he had mentioned at the meeting of the Board of Governors in 1986.

Discussions had recently been broadened to include the KfW, the Crédit National, IMI, and the Caisse d'Epargne de l'Etat de Luxembourg ; and the proposal before the Board involved these organisations as well as the EIB. The CHAIRMAN had hoped to ask Messrs. BRANTNER, SAINT-GEOURS and ARCUTI of the above institutions for their remarks, but Mr. BRANTNER was absent and the two other had been obliged to leave the meeting, given the late hour. Mr. ARCUTI had, however, left a written statement (see below).

The proposals, stressed the CHAIRMAN, implied no derogation from the high standards upon which the Bank had always insisted ; its normal standards of technical, economic and financial appraisal would be maintained, as too would the quality of its portfolio. The object of the scheme was to enable the Bank to make loans to good promoters of sound projects who for one reason or another were unwilling or unable to offer guarantees of the kinds that the Bank had traditionally required. The promoters in question were primarily industrialists in the private sector, including small and medium-sized enterprises ; and the projects would be chosen for their particular interest to the Community. The Management Committee wished the financing of new technology, indeed of innovation in all its forms, to feature prominently among the projects to be guaranteed under the new arrangements.

The proposals were still at an early stage and to some extent tentative. The Management Committee, however, attached great importance to making some such scheme operational in the near future and to making a success of it.

The talks with the three institutions, said the CHAIRMAN, had gone well : IMI and Crédit National had by and large accepted the proposals, though not unconditionally, while KfW, while adding a number of riders, had nevertheless been favourably disposed towards the general concept of the Guarantee Fund.

Mr. SAMUEL-LAJEUNESSE endorsed this position, welcoming the thinking behind the initiative as a contribution to enhancing the role of the Bank. Matters of detail would still, however, have to be worked out.

The CHAIRMAN then read out the written statement left by Mr. ARCUTI who fully endorsed the concept underlying the proposal for the establishment of a Guarantee Trust.

The financial setting had changed radically over the past few years. It was now characterized by fierce competition stemming from greater market activity, from the appearance of new intermediaries, from the greater scope now afforded to pre-existing intermediaries, from the global liberalization of services. Entrepreneurs had acquired innovative industrial and financial capacities. It was now possible for entrepreneurs to address the market directly and ask financial counterparts to provide services that matched the increasing range of corporate needs. Even the most traditional financial instrument - the loan, which was still the linchpin of the system - was being modified and afforded a wider range of options in terms of maturity, currencies, rates and prepayment.

Given the innovative trends in industry and finance, entrepreneurs generally turned to the Bank and to other financial institutions with increasingly far-reaching projects and demands. In addition, often the only guarantee put up consisted in the applicant's equity and the soundness of the investment project submitted.

The Bank had an alternative. It either decided not to participate, possibly penalizing the implementation of projects which could otherwise promote overall economic productivity, or it looked to new funding solutions according to the principles and provisions envisaged in the texts governing its activity.

The Bank's Departments had carefully considered all the possible solutions with a view to providing support for projects which were clearly sound and submitted by good promoters, but without traditional guarantees.

The proposed solution was considered the most appropriate. Mr. AKCUTI endorsed the project's basic philosophy and greatly appreciated the analytical study conducted. He would, however, abstain on this item of the agenda since he had been proposed as a member of the "Trust Committee".

He would accept the other Board members' decision on this point, but wished to stress his personal conviction that the establishment of the "Guarantee Trust" would not impinge upon the decision-making capacity of the Bank, since the latter would preserve its full autonomy and sovereignty even vis-à-vis those projects for which the Trust would have to provide its guarantee.

The specific function of the Trust Board would be to evaluate the composition of the Trust's portfolio - according to its operational regulations - to ensure sectoral and regional risk diversification.

Mr. DE VRIES wholeheartedly agreed that in certain circumstances it would be appropriate for the Bank to assume greater risks, especially when market conditions were less conducive to its operations, but was surprised that the scheme in the Document had not been put forward on a trial basis. The annual ceiling of 700m ECU's and the limit on individual

projects of 150m ECU's he found excessive, and would have preferred the guarantee arrangement to have been tried for perhaps just one year with only smaller firms. He wished also to have more information about the possibilities for reinterpreting the Bank's Statute, the actual funding of the proposed guarantee scheme - whether or not out of EIB surpluses - and the possibility of problems arising in the area of "additionality", and the danger of Governments or other potential guarantors not participating in projects that the Bank backed under such a scheme. He was also somewhat concerned about the apparently privileged position that was to be occupied by those institutions who were to be involved in the Trust Fund administration.

The CHAIRMAN made it clear that the idea behind the Guarantee Fund was not to enable the Bank to move into higher-risk fields, but to enable more promoters to do business with the Bank. The aim was also to offer access to EIB financing to SMEs, advanced-technology firms and other categories of borrower, to overcome the limitations of the existing guarantee system. The proposed scheme was seen as the only possible solution compatible with the Statute.

Mr. MARTINEZ-MENDEZ was generally in favour of the idea of the Trust Fund, but wished to know what ideas had been formed as to its potential costs and profitability. He wished also to know what possibilities there were for other Community long-term credit institutions joining the Trust Committee and - a point made also by Mr. McCUTCHEON - why there was an apparent preference being accorded to those institutions that had been invited to sit on the Committee.

For many Directors, a key consideration was the legal status of the proposed Fund and the statutory implications of the scheme. Mr. FARUP-MADSEN questioned whether the Fund had legality and how it could be reconciled with the terms of the Statute, in particular Article 23. Mr. MEULEMANS was similarly concerned about the nature of the link between the Fund and the Bank, in particular over the prerogatives of the Board of Directors, which to his mind had clear power of decision in regard to guarantees under Article 21 (3) of the Statute. It seemed to him that the Board was being asked to relinquish this function. A trial period might be preferable. He considered that modifying the Statute was a possible option, although most Directors, for instance Mr. MUIER-ENDERS, felt that the matter was more a question of interpretation of the Statute: whether or not this would be as difficult as implied in § 2.2 was debatable.

Mr. RITCHIE spoke for certain other Directors, in particular Mr. McCUTCHEON and Mr. LAVELLE, when he referred to his feeling of unease about the scheme, which he saw in terms of a Committee created by the Bank, a Fund financed by the Bank, Committee members appointed by the Bank and projects put forward for guarantees by the Bank. This he found too transparent; a sentiment shared by Mr. MEULEMANS who spoke of the "window dressing" aspect of the scheme. Mr. LAVELLE described it as an effort to circumvent the Statute, with the Bank guaranteeing itself, and found he could not accept the underlying flavour of the proposals. Mr. HECK encapsulated the problem: if the Bank was not able to lend without guarantees, it was impossible to see how it could pay into a fund to guarantee its own loans.

Mr. McCUTCHEON cited certain of the details of the scheme that were giving him cause for concern. He asked why the other institutions which were to participate in the arrangement and hence enjoy a certain priority for projects on their territory, could not contribute to the assets of the Fund. He wished to know what would happen to the EIB resources deposited with the Fund in the event of its being wound up. He also cautioned against restricting the activities of the Fund, e.g. to high-technology projects.

Mr. MULLER-FENDERS, who welcomed the initiative, also however had a number of specific questions to put. He wanted to clarify whether the risk element was to be borne by funds made available by the Bank, as opposed to the Bank itself; whether the Fund would feature in the Bank's profit and loss account; how the liquidity position would be affected; whether funding the scheme would constitute anticipatory write-off for future losses - an option not open to normal banks - and whether the members of the Trust Committee would carry responsibility for their decisions as Directors of the Bank or representatives of their respective institutions.

Mr. LAVELLE wanted to know more about the rôle of the Trustees; the status of the Fund in terms of avoidance of subsidisation; the grounds for supposing that its facilities would be more attractive than those of commercial banks; the nature of the deposits used to float it, whether preference shares, equity investments or simply some form of funding, and what would be the nature of the deposits used to supply it. He did not, however, object to the possibility of amending the Bank's Statute, if necessary, although given the burdensome and time-consuming nature of such an exercise, he considered that it might be preferable to proceed to any such amendment in the context of the ex novo arrangements to be entered into for the purpose of the Single European Act (see item 11).

Invited to comment on the points so far raised, Mr. McCLELAND, Associate Manager, Research Directorate, explained that to feed the Trust at the outset a deposit of the Bank's liquid funds would be made, to cover possible initial shortcomings in its resources. The intention would be to make the Fund self-financing through the charging of a premium, probably in the range of 20 to 40 basis points. The EIB funds deposited with the Trust would neither be equity capital nor a loan, but simply a placing of liquid funds to see it through its start-up period. He also made it clear that the references made to guarantees for the institutions involved in operating the Fund concerned only those accorded by the Bank in the normal course of its business: there was no question of their being borne by the Fund, the sole purpose of which would be to guarantee EIB lending. The members of the Trust would not therefore be liable: the Trust would be meeting the guarantees given by itself, while the EIB would be guaranteeing, if requested, the lending provided by the institutions participating in the Trust Committee.

The CHAIRMAN stressed that the object of the exercise was not to circumvent the Bank's Statute, but, he reiterated, to take on business that would not otherwise be possible. There was no additional or incalculable risk involved. The Guarantee Trust, as the Bank's Legal Directorate had determined, offered the only way of achieving that end without altering the Statute.

Mr. MEULEMANS commented further on the difficulties involved in the scheme : a trial could perhaps be based on the earmarking of a certain volume of the Bank's reserves as the counterpart for the Guarantee Fund, but he was uncertain how acceptable this might be, for instance, to the Bank's external auditors. The same might go for apportioning part of the 3 000 million ECUs or so of the Bank's paid-in capital, as such. He noted that the proposed Fund was to be launched with liquid funds rather than out of the Bank's reserves and was to be maintained thereafter by premium income, but was concerned about what might happen if the Fund were drained at an early stage through adverse circumstances and the need arose to make further deposits to keep it going. There was a similar uncertainty over the payment of running costs. Mr. MEULEMANS felt that the Document as presented constituted an interesting approach to the problem, in need of further analysis and amplification, with the question of modification/reinterpretation of the Statute more fully studied and expounded. He felt that there was a consensus in the meeting over the need for wider means of guaranteeing the Bank's operations, and that, notwithstanding the legal, political and legislative problems involved, "where there was a will there was a way".

Mr. MOLTRECHT was of the opinion that the Bank had not considered fully enough the option of resorting to greater flexibility in the use of the existing guarantee system referred in §3 of the Document. He felt also that it would be in the Bank's interest to confer with the rating agencies before taking any new step, to ensure that it would not be jeopardising its standing by embarking on such a course. On behalf of Mr. BRANTNER, he emphasised the importance of ensuring that the Fund, if established, did not lead to increased competition with other financing institutions : it should, as stated in §6.1, be an additional mechanism, and not one that would place the subsidiarity of the Bank's role in question.

The CHAIRMAN, summing up, endorsed Mr. BARLEBO-LARSEN's acknowledgement of the need identified in the Document for the Bank to enhance its rôle through wider guarantee arrangements. He accepted also that more clarification was required and further consideration of the ways and means whereby the new arrangements could be made to work. The main objective was to make more projects financable by the Bank. There

was general agreement in the Board, he noted, as to what Mr. LAVELLE called the desirability of finding a way around the guarantee problem, but the question of the instrument whereby such a way could be exploited - whether the Guarantee Fund as proposed or some other device - remained to be resolved. The issue would now go back to the Bank's experts for further consideration and later submission to the Board of what he trusted would be a creative solution based on the considerations raised during the meeting.