Proceedings: EIB–Banque de France conference on:

“Reactivating the Investment Channel”

Held at the Banque de France Conference Centre 10 March 2017

All photos: Banque de France

Banque de France and the European Investment Bank organised a conference “reactivating the investment channel” in the conference centre of Banque de France in Paris the 10 March 2017.

In their key note speeches, Governor F. Villeroy de Galhau and VP A. Fayolle introduced the topic. The discussions unfolded with three panels. D. Revoltella summarised the discussions in her closing remarks.

F. Villeroy de Galhau (BdF) opened the conference by recalling the consensus on the weakness of investment in Europe and praised the supporting role played by the EIB in the context of the investment plan for Europe.

Despite the ongoing recovery, there is still an investment gap in Europe[1] and the saving glut is now not anymore related to high savings in emerging market economies but low investment in developed economies. Contrasting with Europe, investment is not a major issue in France where it is relatively strong and well positioned.

The questions is how to boost investment, what why and how? Three main reasons were developed: the insufficient expected demand, the need to stabilise and clarify fiscal and regulatory norms, and the nature of external financing.

The latter is very important as European corporates suffer from the underdevelopment of own funds. Being at the technical frontier, their investment is based on innovation which implies risk and therefore capital financing –

[1] Some estimates put the gap at around 350 bn.

while conversely catch-up growth is more prone to debt finance. Hence equity finance is core for Europe and very much lagging behind the US. There are several reasons for this: the increase in the equity risk premium which has pushed up the cost of equity, the fiscal treatment with debt cost being deductible, the structure of savings and the regulation surrounding it. The Governor concluded his speech by calling for structural reforms in the context of a financing union which would develop synergies between EFSI and the CMU.

In his keynote speech, ***A Fayolle*** (EIB) showed some of the key results of the first round of the EIB investment Survey, EIBIS. The survey, based on 12.500 EU corporations, sheds some light on the drivers behind the investment gap in the EU. Besides investment gap in several EU economies, investment quality strikes as a major issue that the EIBIS enables to illustrate. In France, the investment share is above the EU and increasing. Moreover, the share of innovation is relatively high. Uncertainty and the labour market regulation are main impediments to higher investment.

A. Fayolle then developed a stock-taking analysis of the EFSI, at “mi-parcour”. The plan aims at financing more risky projects using EC and EIB risk guarantees and internal advising services. From the EUR 315bn expected, more than half have already been signed. As a ratio to GDP, the allocation of the funds related to the investment plan for Europe appears balanced across EU countries. To be more concrete, A. Fayolle then presented some recent EIB operations conducted in France under the umbrella of EFSI, among others, one related to the modernisation of building for increased energy efficiency and another for the restructuring of industrial sites.

A discussion took place regarding the role of the confidence in the financial system to support investment, the impact of Solvency II on insurance companies’ capacity to invest. It was concluded that, while SMEs face more adverse financing constraints, on average, they are not the main problem. But, as they come bigger, they may face a threshold effect, as shown by analysis. The role of the quotation of small enterprises operated by Banque de France as a public service supporting SMEs along their life cycle was emphasized. At the European level, the issue was to transform the capital market union and the investment plan for Europe into instruments for long-term investment.

The first panel session “Investment in France – achievements, gaps and remaining challenges”, was moderated by M.O. Strauss-Kahn (Banque de France)

M.O. Strauss-Kahn introduced the topic by recalling the methodological aspects surrounding the measurement of investment and concluded that nonetheless we can say that investment is low in Europe, but not in France. Investment to value added in France has been above that in Germany since 2002 (since 2011 for productive investment only), while investment in intangibles is much higher in France.

N. Valla (EIB) detailed the results of the EIBIS for France, stressing the potential need to renew the capital stock more than expand production capacity. In his presentation, **F. Lenglart** (France strategy) agreed that the level of investment is not an issue in France but content/quality may be. There may be needs to invest more in the long-term and in human training. Based on a simulation exercise, **X. Ragot** (OFCE) showed that if anything in fact since the crisis, investment in France had over performed. He also showed how the rise in the profit rates of NFCs recorded recently in France.

The second panel session "Investment initiatives: small and smart or a Marshall plan for Europe?", was moderated by P. Jaillet (Banque de France)

P Bérès. (EP) shared some scepticism about the capacity of the EFSI to support convergence, as it favours high quality investment. She stressed the key opportunity of the environmental transition. Finally she argued that EU budget was necessary to support convergence, mitigate asymmetric shocks, and implement a countercyclical policy. She also argued that the structural funds should be reallocated to a fund to ensure convergence.

O. Garnier (SG) detailed the geographic disequilibrium in savings and the return of the Feldstein Horioka paradox. He stressed that, apart from a couple, banks in Europe were not European and remained national. Savings are too much into bank deposits and not enough on equity. He also made the point that the CMU was biased towards market (favour debt more than loans) and not considering enough the capital issue, the underdevelopment of equity in Europe.

L. Menard (CGP) praised the effort to understand investment behaviour and recalled that the investment gap was sourced in few countries, affected by the sovereign debt crisis, and concerned mostly households and government. He agreed that fiscal consolidation negatively impacted investment. Based on the example of high debit installations for which the Junker plan provides part of the financial support thereby reducing the need for public investment/subsidies, he proposed to reallocate part of the EU budget towards higher leveraged investment.

An exchange followed on the need to consider the change in growth regime, and to implement strategic planning to shift upward economic trend growth.

The third panel session "Investment finance, innovative finance and the role of public funds?", was moderated by N. Valla (EIB)

T. Deau (MERIDIAM) explained that public demand could be a key element for investment, beside Innovation necessity, as there seems to be a lack of good projects.

M Bussière (BdF) presented the key results of several analyses: a study which disentangles the factors behind low investment shows that expected demand comes first followed by capital cost and uncertainty. A study on cross-border capital flows shows a reduction in international capital flows as well as a change in their composition.

E. Delaveau (Partech) provided some insights from an investor viewpoint: insurance companies have a role to play on equity investment, especially unquoted. The cost of creating new companies has diminished in Europe. It is much easier to purchase innovation. Finally an entrepreneurial spirit is emerging in French “grandes écoles”.

A. Fürstenberg (EIB) described the implementation of the Junker plan in France as well as some new EIB products. It is well developed and very much concentrated on corporates owing to research champions. What is at less developed is project finance which is still in its infancy. Blending offers interesting opportunities. Looking forward, there is a potential to improve on risk sharing products, energy efficiency products, and products related to social housing.

D Revoltella (EIB) concluded the event

She praised the content of the discussions and summarised the main themes. The recovery in investment takes place but it is weak and fragile so that EIB and policy makers still need to continue taking supportive actions. Government investment remains weak. Business investment requires profitability and should be tilted towards quality more than quantity. Skills mismatches call for specific policies. Finally, the role of regulation and business environment is key. D. Revoltella thanked the organisers.