European Investment Bank
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EUROPEAN UNION
Committee of the Regions

# The role of EFSI in financing urban and regional projects

## The European Fund for Strategic Investments (EFSI): a tool to accelerate investment in Europe

## Factsheet

**An online course (MOOC) for regional and local authorities**

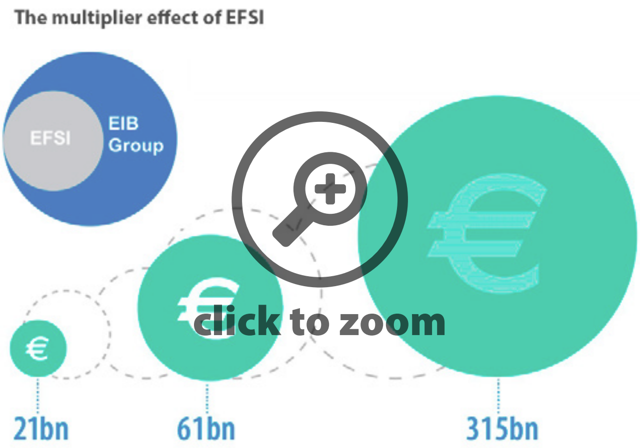
The Investment Plan for Europe is a policy initiative launched by the European Commission in 2014 that **aims to break the vicious circle of declining investment-spending and potential growth and contribute to improving Europe's competitiveness**. The Plan includes an important financial component called the European Fund for Strategic Investments (EFSI) within the European Investment Bank (EIB) Group.

EFSI is not a "fund" in the traditional sense, but rather a guarantee instrument allowing the EIB to increase its risk bearing capacity to lend to sound but higher risk projects, enabling such projects to go ahead. A EUR 16 billion guarantee has been provided from the EU budget and complemented by a EUR 5 billion allocation of the EIB's own resources. This EUR 21 billion funding is leveraged in two ways:

- through an **internal multiplier** the initial endowment of Euros is multiplied so that the EIB can lend out many more Euros
- through an **external multiplier** each loan in turn will generate investment worth several times the loan itself through attracting ("crowding in") third party co-investment

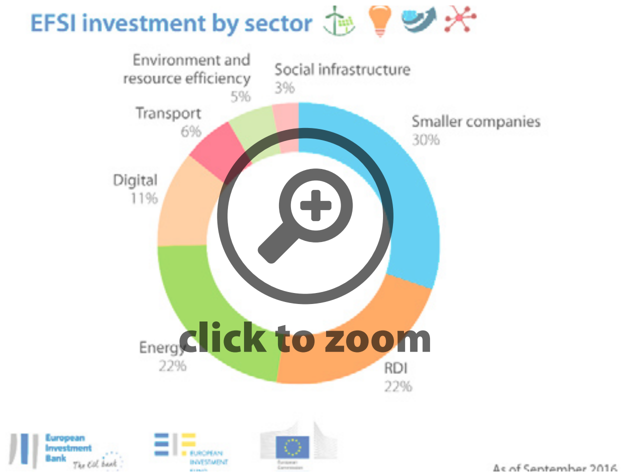
This is illustrated in the picture below. It should be noted that the EU guarantee is portfolio based, and not project by project, so the multiplier will vary from project to project, but overall, a multiplier of 15 appears realistic based on EIB experience.

EFSI therefore aims at **mobilising EUR 315 billion of investments by mid-2018** to help restore EU competitiveness and increase growth and jobs.




Each EFSI project is examined carefully in terms of its multiplier effect, to ensure that on average the EIB financing under EFSI will achieve the multiplier anticipated, as well as its additionality. In September 2016, the European Commission has formally proposed the **extension of EFSI to a total of EUR 500 billion to be achieved by the end of 2020**.

The EFSI focuses on strategic infrastructure such as digital, transport and energy, education, re-



search, development and innovation, expansion of renewable energy and resource efficiency, and support for smaller businesses and midcaps. The EIB Group has proven expertise in these sectors and the capacity to deliver a positive impact on the European economy.

## Complementarity between EFSI and traditional EIB financing

With EFSI support, the EIB Group will ensure additionality by helping to address market failures or sub-optimal investment situations, provide funding for viable projects but with a higher risk profile than projects supported by EIB normal operations. Even though the EIB Group has been supporting higher risk projects for a long time, **EFSI provides additional risk bearing capacity to dramatically increase the scale of the operations**, in terms of number of operations, volume and complexity. This will foster a better use of scarce public resources, diverting them from grants/subsidies to loans/guarantees and enhancing the multiplier effect of investment.

In short, EFSI provides the EIB Group with the capacity and opportunity to:

- **Explore new market**s and serve new clients that were previously considered too risky
- **Develop new financial products** for existing and new clients that are better suited for more complex and riskier projects (e.g. subordinated debt, capital market instruments, credit enhancement instruments)
- **Design new forms of cooperation** (e.g. investment platforms, coordination agreement with National Promotional Banks, co-financing with Sovereign Wealth Funds and other institutional investors) and of blending with EU funds, including European Structural and Investment Funds (ESIF) managed by the EU managing authorities at national or regional level

## The role of EFSI in financing of multisector urban and regional projects

Urban and regional development projects are two important components of EIB financing activities and they have traditionally been targeted by a number of different financial products.

**Direct investment loans** can be used for specific large urban and regional development investment projects, generally with a total project cost in excess of EUR 100m, for which all the components are already known and can be appraised upfront. Examples of such projects may be a metro or a complex urban regeneration intervention.

However, in most cases, cities and regions typically work with 3-5 year capital investment programmes encompassing a large number of relatively small schemes (total individual project cost lower than EUR 50m). In general, final approval to investments is given by the City or Regional Council on an annual basis and all of the details concerning the different schemes to be financed are not known in advance. Moreover, municipal or regional investment programmes often cover a broad range of sectors, such as the construction and/or refurbishment of public buildings, social and affordable housing or social infrastructure (e.g. schools, hospitals, sport and leisure facilities, cultural centres, public green areas, etc.), urban transport, energy efficiency and renewable energy, water supply and wastewater and waste management. Taking into account all of these considerations, these types of investments are better catered for through **multisector framework loans** provided to:

- **Regional authorities** responsible for infrastructure investment at the regional level;
- **Municipal authorities** for large and medium-sized cities (generally with a population of more than 75 000) with sufficient in-house capacity to manage the loan and sufficient critical mass of investment needs under its medium term capital expenditure plan; or
- **Financial intermediaries** (e.g. promotional or commercial banks) who will then extend loans

to smaller municipalities on pre-defined conditions, agreed with the EIB.

Finally, the EIB can also provide **equity investments** in funds which will create a portfolio of new investments in urban and regional infrastructure as well as on specific market segments such as urban brownfield redevelopment.

By increasing the EIB risk-bearing capacity, EFSI increases EIB's flexibility in financing viable projects by taking additional risk, for example relating to the risk profile of the borrower, the investment size, the security available for the project or risks associated with the project itself. This implies that, **through EFSI, the EIB could reach borrowers and counterparts who did not previously have access to EIB financing regardless of the technical and economic merits of their projects**. New potential borrowers may include:

- Cities or regions with lower credit rating (e.g. municipalities or regions whose credit rating is limited by the national rating to sub-investment grade);
- Municipal or regional companies (e.g. utilities, transport companies, private social housing companies) with limited recourse to public sector guarantees;
- Companies or structures owned by associations of municipalities;
- Investment funds with an enhanced risk appetite (e.g. long tenor, long-term investment strategy, focus on very specific sectors such as brownfield decontamination and redevelopment);
- Financial intermediaries with lower credit rating, including those selected to implement financial instruments using European Structural and Investment Funds (ESIF);
- National/Regional Promotional Banks or commercial banks through risk-sharing structures;
- Investment platforms.

The table below provides a few examples of urban and regional development projects that were recently approved by the EIB Board of Directors and the EFSI Investment Committee.

## Examples of urban and regional EFSI projects

| Financial product | Project title | Description | Counterpart |
|---|---|---|---|
| Frame-work loan | Lisbon Urban Renewal Housing Climate Framework Loan | Multisector loan to co-finance a strategic multiannual investment plan (2016-2020) of the city of Lisbon. The operation includes flood alleviation and prevention, urban regeneration infrastructure and social housing, the latter comprising new housing and repairs in existing stock.<br><br>Long-term funding matching the long economic life of the various components of the project is currently not available in Portugal. The operation (up to 30 year loan) would therefore address a market failure in Portugal (municipalities do not have access to the capital markets and Portuguese banks are unable to provide such long-term finance to cover the funding needs of this project). | Borrower: municipality with lower credit rating |

| Financial product | Project title | Description | Counterpart |
|---|---|---|---|
| Risk-sharing | French Overseas Territories Economic Development | The project is an unfunded linked risk sharing for small scale infrastructure and private sector operations financed by the *Agence Française de Développement* (AFD) in the French Overseas Territories that are part of the EU. These regions are lagging substantially behind the French mainland and large parts of EU 28. They lack financing for important infrastructure and show v ery limited private sector investments. Due to higher transaction costs associated with the remoteness of the areas, other long-term financing sources beyond those provided by AFD are scarce.<br><br>The EIB acts as guarantor, alleviating AFD's risk bearing restrictions and facilitating the project approval process within AFD and the financing of the projects. Individual projects will focus, among others, on social housing, renewable energy production, and information and communications technology (ICT). It will hence improve residents' quality of life. | Guarantee beneficiary: National Promotional Bank |
| Service company loan | Poznan Affordable Housing | The project comprises investment in the construction of some 1 300 new affordable housing units for rent in the Polish city of Poznan.<br><br>The EIB loan is direct to the unrated Poznan municipal housing company, without a guarantee of the city of Poznan. Although the project is considered financially sound, it involves a level of risk higher than typical municipal loans to Polish cities. | Borrower: municipal housing enterprise |
| Equity | Ginkgo Fund | The EIB provides a EUR 30m equity investment in a fund with total fund size of EUR 120m investing in contaminated former industrial sites. The fund targets approximately 12 investments in France and Belgium, where it will carry out environmental remediation activities and sell the upgraded property for further real estate development.<br><br>The fund will contribute to circular economy by bringing back brownfield sites into economic use and will foster a more efficient utilisation of space at the urban and regional scale by reducing urban sprawl. | Fund: specialised investment fund with enhanced risk appetite |
| Mezzanine loan | CAP TRI Fund | The CAP *"Troisième Révolution Industrielle"* ("CAP TRI") Fund is an ESIF/EFSI regional investment platform with EUR 37.5m supported by the 2014-2020 European Regional Development Fund ("ERDF") in the Nord-Pas-de-Calais region in France. The EIB contributes to the investment platform with a quasi-equity loan of EUR 20m, using the EFSI guarantee. The fund invests equity and quasi-equity into SMEs, midcaps and Special Purpose Vehicles (SPVs) who are delivering energy efficiency and circular economy projects. It is expected to generate a portfolio of investments of EUR 200m in total. The CAP TRI Fund is the first public-private financial instrument combining resources from ESIF, EIB funding guaranteed by EFSI and private investors. | Borrower: regional investment fund |

## Frequently Asked Questions

### How much money is in the EFSI fund and where is it kept?

EFSI is not a "fund" in the traditional sense but a guarantee instrument allowing the EIB to increase its risk bearing capacity to lend to higher risk projects or borrowers, enabling such projects to go ahead. EFSI is endowed by EUR 16 billion guarantees coming from the EU budget and EUR 5 billion of EIB own resources. It is structured so as to be able to mobilise a total of EUR 315 billion of investment by mid-2018 and EUR 500 billion by the end of 2020, including funding "crowded in" to projects from private and public sector sources alongside EIB EFSI-backed funding. EFSI has been integrated into the EIB Group and projects supported by EFSI are subject to the normal EIB project cycle and governance.

### How can cities and regions apply to get EFSI funding?

Cities interested in receiving EIB funding, whether backed by EFSI or through standard EIB lending, should contact the EIB through the normal channels (via forms on the EIB website and via EIB offices located in the Member States). In our experience, cities and regions are interested in obtaining funding for their projects regardless whether it is standard EIB loan financing or EFSI-backed EIB loan financing. If a city or region is interested in EIB financing the EIB loan officers analyse the risk profile of the borrower, assess the project and make a recommendation to the Bank's management (and, if appropriate, to the EFSI Investment Committee) as to the nature of the financing to be provided.

EFSI offers possibilities for borrowers or structures with a higher degree of risk to be financed than was the case in the past. For example, standard EIB financing has typically required regional/municipal guarantees or bank guarantees for lending to regional/municipal companies, or for such companies to have investment grade credit ratings. With EFSI, under certain conditions, EFSI-backed loans can be made to such companies with more limited forms of security. Similarly, EFSI may facilitate a greater number of EIB investments in financial intermediaries who are selected to deliver financial instruments with ESIF.

### If EFSI projects need to be repaid, how can they be used to finance urban or regional roads or other non-revenue generating investments?

EFSI is well suited to projects which generate own revenue and can be financed on a "project finance" basis with loan repayment coming from the revenues generated by the project. However, EFSI can also enable public sector financing for non-revenue generating projects through recourse to the balance sheet of a regional/municipal company with enhanced credit risk.

### Can EFSI funding be combined with ESIF funding for the same project?

The EC has recently issued a guide on combining EFSI and ESIF funding. Combinations are possible for either individual projects or at the level of financial instruments, provided that the expenditure item included in a request for payment for reimbursement by ESIF does not receive support from another fund or Union instrument. This means that EFSI funding cannot be considered as the national co-financing contribution to co-finance an ESIF grant and that the EFSI-supported part of the project cannot be declared as eligible expenditure for ESIF.

### As EU funding has been put into EFSI, does this mean there is less funding under the ESIF? Is the EFSI going to grow until ultimately there will be more EU funding provided under EFSI and other financial instruments and less grant funding?

The role of financial instruments has been increasing under the EU structural funds over the past two programming periods. In the 2014-20 programming period financial instruments have been mainstreamed into the regulations. It also appears, as announced in September 2016, that EFSI will be extended and increased in size during the present programming period. Cities and regions typically see a trade-off between simpler grant financing and more complex higher risk structures involving financial instruments while, at the same time, recognising the value or the revolving nature of financial instruments as opposed to pure grant financing. Some Member States are considering the possibility to re-invest the proceeds of investments made under previous financial instruments, such as JESSICA urban development funds established in the 2007-13 period. In a world where public financial resources are increasingly scarce, it would appear prudent for cities and regions to experiment with revolving financing structures to finance revenue-generating projects, thus dedicating grant resources only to investments which could not be financed in any other way.

**Is EFSI funding by EIB considered to be state aid?**

No, EIB funding under EFSI (or regular EIB funding) is not considered to be state aid. However, the EIB does look at the overall funding of a project to check whether there is state aid from one of the other co-financiers.

**How much does EFSI funding cost compared to regular EIB funding?**

EIB funding under EFSI does price in a margin for the additional risk incurred, but this will depend on the particular credit risk of the operation.

**Is EFSI funding just for private sector projects?**

No, EFSI funding can also be provided to public sector borrowers and their projects, where there are enhanced levels of risk as compared with traditional operations (see table "Examples of urban and regional EFSI projects").

**Are some projects which could not be financed by EIB due to eligibility restrictions now eligible for funding under EFSI?**

No, projects must meet EIB general eligibility criteria, and then some of these projects may qualify for EFSI under the EFSI eligibility criteria. For example, tourism is an eligible sector under EFSI, but under EIB standard eligibilities hotels are eligible mainly in less developed and transition regions; the fact that tourism is eligible under EFSI does not make hotels become eligible in developed regions.

## For more information

- How can the Investment Plan for Europe be mobilised to support investment in cities?
- How can the funding under the Investment Plan for Europe be combined with EFSI?

Video interviews with Gerry Muscat, Head of Urban Development, EIB

**Disclaimer**

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