***Summary of the Joint Banco de Portugal and European Investment Bank Conference: "Investment and investment finance: Funding Growth and recovery – Portuguese challenges in a European context*"**

Monday 4 December 2017, the conference "Investment and investment finance: Funding Growth and recovery – Portuguese challenges in a European context" took place in Porto. The memo summarises the content of the presentations and discussions.

Carlos Costa (Banco de Portugal) introduced the event with welcome remarks. He stressed the importance of the North region in the export activity of Portugal. For almost forty years, the EIB has been a key partner to support economic development, and in 2016, its support amounts to around 1% GDP. Looking ahead, technological change, digitalisation, and raising productivity are the main challenges. Lack of finance for innovation and the need to diversify sources of finance are key issues in this regard. Portuguese firms need more capital to deleverage and better management.

Debora Revoltella (European Investment Bank) provided an overview of the EIB investment report and survey focused on Portugal. In this country, the challenge is to ensure that the current recovery matures into sustainable growth. She structured her presentation along three parts. *First*, regarding overall investment, corporates capex leads the recovery, while public investment ratio to GDP is among the lowest in the EU. At time of fiscal consolidation, an increased public support to the economy requires strengthening ex ante assessment, and adopting more efficient decision rules. The municipality survey of the EIBIS2017 shows that there is room for improvement in Portugal. *Second*, the gap in investment has a lot to do with quality. Corporates invest mostly in replacement and not enough in intangible. This impedes resource allocation as well as the capacity to take risk and innovate. *Third,* while access to finance is tighter in Portugal, what seems to matter more is the right form of finance. This explains why corporates are constrained: mostly because they are dissatisfied with the collateral requirement and the cost. The policy agenda should focus on increasing the variety of forms of finance and especially those helping investing in innovation. However, less than 1% of the firms surveyed want more equity, and this show that a lot needs to be done.

Alberto Castro (Institution for Financial Development) introduced the first panel "Financing investment in the recovery – challenges in a European context", moderated by **J. V. Pereira** (Expresso Journal). Investment is key to potential growth and quality matters as much as quantity. Therefore, public policies should also aim to improve investment in intangibles. Developing investment requires a strategy and changes in the domains of SMEs finance or Venture Capital are needed. At the same time, foreclosure of companies has a social cost in terms of skills lost and capital scrapped. Hence, the Capitalizar project which aims at helping corporate restructuring.

Gabriela Figueiredo Dias (Portuguese Securities Market Commission) stressed that changing for equity requires more transparency and financial literacy. It has high cost and requires complying with complex regulation. Simplifying administrative procedure and reducing red tapes may help, especially for SMEs.

Isabel Furtado (TMG Automotive) emphasized that innovation can take place even in traditional industries such as textile, thereby enabling the company to become trend setter. However, these industries are affected by stigmas or have a bad image from financiers. More generally, when asking for external finance, there is a lack of understanding of the industry from the partner – Mrs Furtado highlighted her appreciation for the industry expertise of the EIB officers – an unparalleled experience in the company's entire history. This is one of the reasons for which corporations revert to bank loans, besides the complexity of joining the stock market.

Guilherme Costa (Phyxius SA) developed the view that institutional changes could result in more support to investment. More must be done to improve the quality of management. The problem is also about skills, not always money. Opening the capital structure to partners outside families can help, as well as helping successions.

Luis Pedro Goncalves (Basi Laboratories) recalled the existence of EIB loans for innovation in manufacturing processes. Commercial banks are not well prepared to setup some products, understand companies or sectors. Scale is key, more concentration and less regulation may help.

In the discussions, the need to recourse to the government was tempered with the need to know more about corporates, to make Portugal more open, able to generate more good projects to sell outside the country. Energy costs are very important elements of competitiveness and more can be done to reduce them. Uncertainty is part of the capitalist system but regulatory uncertainty should be reduced.

Carlos Caldeira (Portuguese National Innovation Agency) introduced the second panel "Supporting investment with innovative policies" which was moderated by A. Aguiar (University of Porto). Portugal needs to invest more" in innovation, while the benefits of innovation are shorter-lived. However, there are many instruments already available at the national or EU level to accompany this investment – although not all companies are aware of that. In fact, the gap is in the capacity to apply research. Risk capital must understand the technological challenges and support dissemination of technology within the economy. Portugal uses all sorts of funds to do that, such as structural/cohesion funds, and setup incubators.

Birthe Bruhn-Léon (European Investment Bank) reminded that the Bank had been a partner in Portugal for almost 40 years, financing projects for jobs, competitiveness, environment and regional developments. Support to SMEs and Midcaps, structurally prevalent in the Portuguese economy and facing tighter access to external finance, has dominated EIB activity over the past years. The sharp decline of public investment in the context of fiscal consolidation calls for innovative financing models that catalyse new public investment while not weighing on the State budget. Utility infrastructure, urban rehabilitation, energy efficiency, along with innovation and skills have become very important areas of support. In technical terms, the financial support is achieved through debt, risk sharing or equity-type instruments. Overall, it amounted to nearly 1.5 billion euros last year.

Carlos Martinez Mongay (European Commission) recalled that Portugal experiences a very strong recovery and that the question is about its sustainability. Demand composition has shifted towards investment and exports which, following the structural reforms should benefit more from the external momentum. However, annual potential growth stands at 1.5%, while GDP per capita is at 75% of the EU average. Investment fell across all sectors during the crisis – particularly public investment (80% of current public investment comes from EU funds). Hence, more investment is needed. The current account is now in balance and to increase investment without more domestic savings, Portugal needs either to go back to external indebtedness or FDI (preferred option, but more difficult). Several barriers limit capital expenditure: high indebtedness, fiscal consolidation, access to external finance and underdeveloped capital market. The need for skilled labour requires further improvements in the functioning of the job market, with possibly more local wage bargaining and less incentives to temporary work. The low speed of the judiciary is also a concern, firms´ entry and exit must be facilitated and several administration processes must be reviewed.

Pablo Milan Cantero (European Investment Fund) focussed on the role of EIF in supporting the development of Venture Capital (VC) and Private Equity. The system has improved and while more needs to be done, it is now possible to raise funds from the private sector. The situation in Portugal differs from that in the Scandinavians' countries where VC investment is supported by pension funds. In Portugal, following the crisis, VC became independent from banks and new partners must be found.

Jose Manuel Mendonça (Institute for Systems and Computer Engineering, Technology and Science) proposed as principles that new policies to foster innovation should be built on old ones and enriched by international experiences. Talking to stakeholders and looking at the complete knowledge value added chain also matters. There is a need to understand the nexus between state, universities, companies and the context. Experience has shown that tax incentive works relatively well. However, there are also lessons from mistakes, disasters. The political knowledge always needs to be rebuilt after elections. At the local level, research projects are much less funded than in Lisbon. The administrative time to treat dossiers is too long and red tape is too heavy. Fixing the salaries too high is detrimental to hiring (in the case of PhD). It is not optimal to put absolute beginners at the head of institutions. To summarise, it is good to listen to the actors, to simplify the processes they have to follow and make them accountable. New policies also require new people.

In the discussions, the need to remain agile was stressed. Renewable energy development and transport infrastructure were taken as examples of successful infrastructure finance, but where financing models have evolved. Reducing NPLs is a necessary condition to enhance the banking sector's ability to supply credit, and looking forward, reactivating the securitisation and covered bond markets may help. Savings in Portugal may be too low but besides encouraging them, attracting FDIs is also a solution, as FDIs bring finance and intangible. Management needs to understand technology, as even traditionally simple industry can become very high tech. There is a need for more people in some segments and opening the numerus clausus for students in some domains may help.

In his keynote speech, **Paulo Ferreira** (Deputy Ministry of Economy) emphasized the challenges of digitalisation. Artificial Intelligence is going to play a larger role, and dissemination of data and cyber security have become hot topic in the policy agenda. Corporate Indebtedness remains a concern in Portugal but the Capitalizar program should help stabilising the financing. Policymakers must deal with something new, and help accompanying the transition. On its side, the financial system must be ready to finance the technological change and understand the needs of the companies.

In his closing remarks, **Roman Escolano** (European Investment Bank) thanked Banco de Portugal for hosting the event and congratulated the organisation committee. As the recovery strengthens, investment needs become more pressing to avoid bottlenecks. He mentioned that our survey shows that the share of corporations that perceive constrains in their access to external finance is particularly elevated in Portugal, and especially for SMEs. That is why in 2016 the EIB Group has provided 1.2 billion euros of support to SMEs´ investment. There is also a need to modernise production capacity and foster intangible investment, notably focusing on the improvement of knowledge and skills. He stressed the importance attached by companies to public policies dedicated at improving professional training and higher education. He concluded by stressing that there is a need to do more and better and that the event was an opportunity for the EIB group to improve its understanding of the investment gaps and shape its support.