European Commission

Improving the take-up and effectiveness of financial instruments

Final Report

Contract No 2015CE16BAT065

Fiona Wishlade, Rona Michie, Patricia Robertson, Philip Vernon

May 2017

EPRC
EUROPEAN POLICIES RESEARCH CENTRE

EUROPEAN COMMISSION

Directorate-General for Regional and Urban Policy
Directorate B — Policy
Unit B.1 — Policy Development and Economic Analysis

Contact: Daniel MOUQUE

E-mail: REGIO-B1-HEAD-OF-UNIT@ec.europa.eu

European Commission
B-1049 Brussels

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2017 EN

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Luxembourg: Publications Office of the European Union, 2017

ISBN: 978-92-79-72117-5
doi: 10.2776/981010

Abstract

In the wake of the financial crisis, public and private investment has stagnated due to loss of confidence and austerity policies. The supply side for investment is complex, with the boundaries between public and private often blurred. The overall landscape varies widely between countries, but is characterised by the growing importance of national promotional banks (NPBs) in economic development. Carefully calibrated financial instruments, often provided through NPBs, can provide sustainable support for revenue-generating / saving projects in areas like SME support, R&D&I and energy efficiency where market imperfections result in suboptimal levels of investment. The uptake of ESI Fund co-financed FIs has increased in 2014-20, but remains focused on loan-based SME support. The regulatory framework for ESIF co-financed FIs has improved, especially through mandatory ex ante assessments, but the implementation of FIs remains challenging for Managing Authorities, suggesting that more timely guidance, more stable rules, and perhaps more 'off-the-shelf' instruments would be beneficial. However, the plethora of initiatives at domestic and European levels can make the FI 'scene' difficult to decipher and quantify. Related, there is evidence of policy competition, pointing to the need to rationalise modes of intervention and tailor FIs to the relevant institutional and economic context.

About this document

This document is the final deliverable of the study on Improving the take-up and effectiveness of Financial Instruments, Contract No 2015CE16BAT065. The study was carried out by the European Policies Research Centre (EPRC), University of Strathclyde.

Disclaimer

Authors of the study

Fiona Wishlade (EPRC)

Rona Michie (EPRC)

Patricia Robertson (EPRC)

Philip Vernon (EPRC)

Acknowledgements

The study would not have been possible without the support of our national experts in different EU member states and our editors whose contributions are gratefully acknowledged. We would like to thank Vainius Bartasevičius, Stanisław Bienias, Aleksandrs Dahs, Dr Tatyana Daskalova, Viktoriya Dozhdeva, Claudia Gloazzo, Iveta Holá, Lucie Jungwiertová, Stefan Kah, Dr Damjan Kavaš, Zsuzsanna Kondor, Timothée Lehuraux, Dr Irene McMaster, Klaudijus Maniokas, Josef Mareš, Dr Carlos Mendez, Dr Georgios Michailidis, Professor Tatjana Muravska, Dr Vinko Muštra, Martin Obuch, Ricardo Pedraz-Gonzalez, Andreas Resch, Gabriela Šulmanová, Cristian Şurubaru, Dr Kristiina Tõnnisson, Dr Arno van der Zwet and Heidi Vironen.

We would also like to thank the representatives of DG Regional and Urban Policy / Policy Development, Strategic Management and Inter-Institutional Relations: Peter Berkowitz, Daniel Mouqué, Ragne Villakov and Andreas Metz, and DG Regio B3 Unit Ieva Zalite.

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Rationales for financial instruments co-financed by the ESI Funds

The planning and early implementation of EU Cohesion policy for 2014-20 took place in the aftermath of the worst financial crisis since the 1930s. The impact of the crisis has been both widespread and long-lasting, and, in general, Europe has been slow to recover. A key factor in the weakness of the recovery has been the impact of the crisis on both public and private investment, in spite of historically low interest rates and high levels of liquidity in European capital markets. The prime cause relates to uncertainty, as well as systemically low rates of economic activity. However, while there is no longer a general problem of access to finance, access to finance remains a serious concern for certain market segments – notably SMEs and infrastructure.

Both private and public sources play an important role in the supply of finance, but are not always easy to distinguish. In many EU Member States, the public sector has long been involved in the supply of FIs to pursue policy goals. The role of national promotional banks became more prominent during the economic crisis, and has continued to grow. Promotional banks can provide FIs directly, but most frequently operate indirectly, often through commercial banks. EU-level sources of funding are also increasingly channelled through these domestic sources.

The justification for public intervention in economic development policy is to support activities that market operators cannot or will not undertake alone, but which are considered in the wider public interest. This is sometimes characterised as 'market failure', but in fact can arise in situations where there simply is no market and the private sector is operating quite rationally, or where the market is imperfect and operating sub-optimally. These include the provision of public goods, the supply of merit goods, the presence of externalities and imperfect information in financial markets. Not all of these types of market imperfection can be addressed using FIs.

Financial instruments offer some advantages over non-repayable instruments (such as sustainability and cost-effectiveness), but must be tailored to circumstances and ultimately can only be used where the investment is income-generating, enabling the initial support to be repaid. In considering forms of intervention and rationales for FIs, it is worth noting that the term 'financial instrument' encompasses very diverse financial products that differ considerably in terms of their suitability for different targets, their implications for recipients and their modes of governance.

In terms of the rationale for using co-financed instruments in Cohesion policy, these are very much context-driven, reflecting the scale and focus of OPs, the appetite to experiment with forms of finance not widely used in domestic policy, as well as the wider domestic financial context.

Evaluation evidence of effectiveness of co-funded FIs is thin and has focused on co-funded FIs for enterprise support; there is little evidence of a revolving effect or anticipated levels of private sector participation. However, there is some evidence of FIs having helped achieve OP objectives, in particular by increasing access to finance – one of the main rationales for using FIs in 2007-13 ERDF OPs. Transferability of lessons on where FIs are most effective is limited by the context-specific nature of FI implementation: evidence suggests that FIs are most effective where tailored to specific regional or national circumstances, as there is no successful 'one size fits all' approach. Models are seldom transferable without modification to take local, regional or national circumstances into account. This can include differences in local economic conditions, in banking and legal systems, previous experience with implementation of FIs etc.

The learning curve of FI implementation over several programming periods provides some evidence of the conditions which support effective FI implementation. FIs are most effective:

- When they are based on an accurate assessment of the market situation
- where there is flexibility and an ability to respond to change
- where there are safeguards against ‘objective drift’
- where they build on previous experience
- aid is well-focused and related to the programme strategy.

The use of financial instruments co-financed by ERDF, Cohesion Fund, ESF and EMFF in 2014-20

According to indicative data in the Operational Programmes (OPs), Member States planned to almost double their spend on financial instruments, from Structural Funds resources committed of around €11.4 billion in 2007-13, to around €21 billion in 2014-20. Plans vary very widely, with four Member States planning to commit more than four times 2007-13 levels (NL, PT, RO, SI), and others planning to reduce or even cease using FIs. Some Member States plan to commit more than 8 percent of OP contributions in the form of FIs (BG, HU, LT, NL, PT, SI and UK). However, under many OPs, the design and implementation of financial instruments remains in a state of flux and the final outcomes are likely to differ from OP plans in significant respects. Changes in plans for FIs are also affected by the outcomes of the ex ante assessments.

In 2007-13, the use of financial instruments was mainly the preserve of the European Regional Development Fund. All Member States that used FIs used the ERDF to co-finance them, with seven also using the European Social Fund. Six Member States used the European Fisheries Fund for financial instruments. The Cohesion Fund could not be used for financial instruments in 2007-13. In 2014-20, planned FI allocations remain predominantly under ERDF, but usage of the ESF and EMFF has also increased - the overall increase in the planned use of EU resources for FIs under the ERDF and the ESF is broadly the same (approaching double).

Analysis of spending plans for FIs shows that more than half of planned FI spend (52 percent) is targeted at SMEs (Thematic Objective 3). A further 17 percent each is aimed at research and innovation (Thematic Objective 1) and low carbon (Thematic Objective 4). This means that around 87 percent of all FI spend is planned for these three objectives.

Some 157 or just over half of ERDF, ESF and Cohesion Fund OPs allocate funds for financial instruments (excluding Interreg programmes, where no OP included plans for using FIs). However, the scale of planned financial instruments varies extremely widely both in absolute terms and in terms of importance within the relevant OP. Fourteen OPs have planned spending exceeding €400m; collectively these account for 55 percent of planned FI spend. Twenty-seven OPs plan to allocate more than 20 percent of resources to FIs. Only five EMFF OPs have definite plans for FIs in 2014-20, for which around €80 million has been earmarked. In addition to the above six Member States have or plan to implement SME Initiative OPs (BG, ES, IT, FI, MT and RO).

Progress in implementation also varies markedly within and between countries. Many Member States are still at quite an early stage in FI implementation (although the picture is continually changing and developing). A significant number of ex ante assessments have been completed (an estimated 143 at the time of writing). The approaches taken to these have been very varied, with some Managing Authorities undertaking ex ante assessments in blocks or stages, and other undertaking updates of existing studies. In addition, ex antes assessments may have been undertaken at Fund level (e.g. for ERDF) either within one OP or across several, for all funds within an OP, for specific instruments or financial products already envisaged or for specific Thematic Objectives. At the time of writing, few FIs were operational – those which were tended to build on previous experience, and largely address support for enterprises.

Practical, legal and administrative issues in the use of financial instruments co-financed by the funds

According to the research carried out for the study, the views of Managing Authorities on the advantages and disadvantages of different form of support (grants vs FIs) are not primarily conceived in terms of pros and cons, but rather in terms of the type project for which they are most suitable. Different forms of support suit different project types – MAs view SME development (TO3), low carbon economy (TO4) and research and innovation (TO1) as most appropriate for FIs.

The key disadvantage of grants is perceived by the MAs to be their lack of sustainability and the risk of creating a subsidy culture, while the key disadvantage of financial instruments is considered to be their administrative complexity. FIs are considered by MAs to be harder to administer than grants due to lack of experience, the quality of the regulatory framework and the associated administrative burden, although financial intermediaries can lessen the administrative burden of FIs. Some MAs also consider that, for final recipients, the administrative burden of FIs is lower than grants.

Value for money has been a growing concern in public policy for many years, and this has led many to question the role of grants to promote economic and social development. Indeed, the notion that financial instruments provide better value for money because sums are repaid and reinvested is one of the key arguments put forward by the Commission for their use. However, value for money is not intrinsic to the form of support - sometimes grants can offer better value for money than FIs, because of administration costs. Among the arguments for financial instruments is that their economic impact can be greater not only because funds are recycled and support more projects, but also because the use of repayable funding can improve project quality. FIs are perceived by MAs to have economic impacts on several levels and sometimes for less outlay than grants.

The term 'financial instrument' has become a 'catch all' for forms of support that are repayable, unlike grants. In practice, however, this term encompasses a variety of forms which may have little in common with one another. The choice of financial product by MAs is driven primarily by the outcome of the ex ante assessment.

The relationship between different forms of support (grants, FIs etc.) is important - unless the various instruments are appropriately tailored to meet policy and market requirements, and dovetailed with one another, there are risks that measures compete, overlap or leave some needs unmet. Competition or overlaps between forms of finance can be minimised by appropriate programme design.

Some Managing Authorities do not plan to use FIs at all, whereas others use or plan to use them under some, or even all, Thematic Objectives. The survey of Managing Authorities sought to understand why financial instruments had not been used. Overall the main stated reasons for not using FIs is their unsuitability for planned projects (e.g. non-revenue-generating); however, under TO3 and TO4, where FIs are most used, the main reason given for not using FIs is the perceived lack of demand among final recipients.

In the 2014-20 Regulations, the Commission introduced the option for MAs to use template FIs which comply with standard terms and conditions (off-the-shelf). The template models are intended to facilitate FI set up; if the template is adhered to, MAs are assured of the compliance of the proposed FIs across a range of regulatory issues, including selection of financial intermediaries, funding agreements, State aid and management costs and fees. Views on off-the-shelf FIs are broadly positive, but uptake has been low due to timing of the Regulation and a desire for greater domestic flexibility. In some cases, the OTS instruments have been used as 'inspiration' to design final products tailored more closely to local needs.

The 2014-20 Regulations underpinning the use of FIs are a step change from those applicable in 2007-13, partly in response to Member State concern at the absence of detail and lack of clarity in those rules in the previous planning period. The general perception of Managing Authorities on the new legislative framework is rather mixed, though it is fair to say that it is generally found to be challenging. Some Managing Authorities were positive on the new Regulations, and the obligatory ex ante assessment is viewed very positively; however the view that the Regulations could be improved was more widespread. A key area of concern is the uncertainty associated with the scope for interpretation.

The legislative framework for financial instruments in 2014-20 has been characterised by considerably increased emphasis on support, notably through *fi-compass*, and on written guidance issued by the Commission. Nevertheless, a significant number of Managing Authorities think that more guidance is needed in certain areas, and three main issues were identified:

- timing: there has often been a significant gap between the regulation being issued and guidance being available
- tailoring: many MAs consider the guidance to be too general for their needs, and often too theoretical or lacking in practical examples and would like more, and more effective, direct contact with the Commission on their specific needs
- status: the impact the guidance can have on audit, and the perception that the Commission sometimes applies stricter rules in the guidance than is implied by the regulations themselves.

In considering what changes to the legislative context might facilitate the use or take-up of FIs, identified factors include changes to the State aid rules, simplification, improved communication with the Commission, training, information and advice.

The relationship between ERDF, Cohesion Fund, ESF and EMFF FIs and EU-level instruments and EFSI

ESI Funds are part of a complex landscape of funding mechanisms, including from private and public, domestic and EU-funded sources and at regional, national and EU levels. MAs can contribute ESIF resources to joint instruments such as the SME Initiative, and may also seek complementarities with other EU-level instruments (often managed by the EIB Group). The CPR makes specific reference to the possibility of contributing (ERDF and EAFRD) resources to the SME initiative. This enables MAs to contribute resources to FIs set up at EU level. So far, uptake of the initiative has been fairly limited; only Bulgaria, Finland, Italy, Malta, Spain and Romania have signed up to it. Part of the explanation for limited uptake may be contextual changes: the scheme was introduced to address liquidity problems in banks but these have been less severe than expected.

There is also a wider set of centrally managed EU-level FIs with which there are potentially important synergies with Cohesion policy activities, including COSME, which aims to improve access to finance for SMEs through loan guarantees and equity; InnovFin, the Horizon 2020 equity sharing and risk sharing instruments for innovative SMEs, and the Connecting Europe Facility, which provides finance for energy, transport and digital projects. Another development at EU level is the introduction of the European Fund for Strategic Investments (EFSI), which was set up by the European Commission and the European Investment Bank as the cornerstone of the new Investment Plan for

Europe. The Commission published guidance on ensuring coordination, synergies and complementarity between the two sources of funds in April 2016.

The relationship between ESI Fund FIs and other EU instruments of various kinds is not well understood by MAs, although where an ex ante assessment has been completed, MAs are better able to form an opinion about the relationships between ESIF FIs and other instruments. These MAs are more likely to perceive there to be competition between ESIF FIs and other instruments than those MAs where no ex ante has been done, and there are concerns about the relationship between ESIF FIs and other EU sources of finance. This concerns, in particular the competitiveness of ESIF FIs and the perception that these are disadvantaged compared to other EU funding sources due to the State aid rules, and to some extent procurement issues. Financial intermediaries generally had a more comprehensive perspective on funding sources, but often agreed that the landscape was crowded and confusing. There are also potential overlaps between ESIF and EFSI supported FIs, and while some think there are opportunities for synergies, most consider these to be highly challenging.

Conclusions and recommendations

The aim of the final section of the report is to provide conclusions on the strengths and weaknesses of the legislative framework established at EU level for the use of financial instruments, and to identify specific recommendations for possible improvements and options for the future regarding the legal framework and the uptake of financial instruments co-financed by ERDF, Cohesion Fund, ESF and EMFF.

The recommendations arising from the study are essentially threefold:

First, there is a need to reappraise the role of Cohesion policy FIs against the backdrop of an increasingly complex intervention landscape. Cohesion policy FIs have specific strengths, such as their capacity to adapt to regional conditions or help develop local financial markets, but the regulatory aspects of Cohesion policy FIs are onerous compared to many horizontal and EU level initiatives, and while 'synergies' between different initiatives have become the 'holy grail' of policy implementation, their achievement demands significant administrative capacity.

Second, there is a compelling case for increased regulatory stability. In both the 2007-13 and 2014-20 policy cycles, discussions about the effectiveness of financial instruments have been dominated by issues of compliance and process, rather than policy design and a focus on 'what works and in what circumstances' to address specific economic development objectives.

Last and related, there is a case for refocusing guidance. The increased support provided has been widely appreciated, but Managing Authorities have been critical of its timing, and its status in relation to audit requirements. More specifically, if FIs are to be more widely used in areas where there is limited experience, more tailored support and exchange of best practice is needed.

The broad thrust of the recommendations outlined above is to consolidate, coordinate and stabilise the regulatory framework for financial instruments and to support the development of administrative capacity in Managing Authorities. Of course, it is also possible to countenance more radical options for increasing the uptake and effectiveness of financial instruments. These could include limiting the implementation of FIs to so-called off-the-shelf models, requiring the use of EU level instruments, ring-fencing a proportion of operational programme allocations for FIs, using only grants under share management, or imposing a presumption in favour of FIs by requiring explicit justification for the use of grants in support of productive investment. In practice, the most effective way forward is likely to lie in combining *elements* of these options, and taking a more nuanced approach that takes account of past experience. In other words, incremental approach to policy change and supporting the uptake of FIs – building on policy experience, learning and the development of administrative capacity, but adjusting policy to maximise the benefits from elements that have or could work well. The use of co-financed FIs has involved the build-up of administrative capacity and of the policy networks needed to facilitate their use. Regulatory stability is essential to consolidate this experience and to enable the focus to shift away from *procedural challenges* and to concentrate on the *substantive change* that FIs can induce. For this, more and better information is needed to enable a fine-grained analysis of which co-financed financial products work and why: concrete evidence of how and where FIs can be effective, and models of 'success', would provide compelling reasons to increase their uptake.

Résumé

Les fondements des instruments financiers cofinancés par les Fonds ESI.

La préparation et les débuts de la mise en œuvre de la politique de Cohésion pour 2014-20 ont eu lieu à la suite de la pire crise financière depuis les années 1930. La crise a eu un impact à la fois large et durable, et la reprise en Europe a en général été lente. Un facteur clé de la faiblesse de la reprise a été l'impact de la crise sur l'investissement public mais aussi privé, en dépit de taux d'intérêts historiquement bas, et de niveaux de liquidités élevés sur les marchés de capitaux européens. La cause première est liée au climat d'incertitude, ainsi que des taux d'activité économique systématiquement bas. Cependant, alors qu'il n'y a plus de problème général d'accès au financement, celui-ci demeure une inquiétude dans certains secteurs du marché – notamment pour les PME et les infrastructures.

Les ressources privées et publiques jouent un rôle important dans l'offre de financement, mais ne sont pas toujours faciles à distinguer l'une de l'autre. Dans plusieurs Etats membres de l'UE, le secteur public est depuis longtemps impliqué dans l'offre d'instruments financiers à la poursuite d'objectifs de politique publique. Le rôle des banques nationales de développement est devenu plus proéminent pendant la crise économique, et a continué à grandir. Les banques de développement peuvent mettre directement à disposition des instruments financiers (IF), mais la plupart du temps les gèrent indirectement, souvent via des banques commerciales. Les sources de financement au niveau de l'UE sont également de plus en plus acheminées via ces canaux nationaux.

La justification de l'intervention publique dans les politiques de développement économique repose sur le soutien aux activités que les opérateurs de marchés ne peuvent ou ne veulent pas entreprendre seuls, mais qui sont tout de même considérées comme étant d'intérêt public. Ceci est parfois identifié comme une « défaillance du marché », mais peut en réalité avoir lieu dans une situation où il n'y a simplement pas de marché existant et où le secteur privé agit de façon rationnelle, ou bien quand la situation de marché est imparfaite et génère un équilibre sous-optimal. Cela inclut la production de biens publics, la production de biens d'intérêt social, la présence d'externalités et des informations imparfaites sur le marché. Toutes ces imperfections de marché ne peuvent pas être corrigées par l'utilisation d'instruments financiers.

Les instruments financiers offrent certains avantages par rapport aux instruments de soutien non-remboursables (comme leur soutenabilité, et leur efficacité-coût), mais doivent être adaptés aux circonstances, et ne peuvent être utilisés que pour des investissements qui génèrent des profits, permettant alors le remboursement du soutien initial. En considérant les différentes formes d'interventions et logiques des IF, il est utile de noter que le terme d'« instrument financier » comprend un ensemble divers de produits financiers, qui diffèrent considérablement en termes de pertinence selon les cibles, d'implications pour les bénéficiaires finaux, et de modes de gouvernance.

Concernant les motivations expliquant le recours aux instruments financiers cofinancés dans le cadre de la politique de Cohésion de l'UE, celles-ci sont particulièrement dépendantes du contexte, en fonction de l'échelle et du focus des PO, de la volonté d'expérimenter de nouvelles formes de financement peu développées dans les politiques nationales et infranationales, ou encore plus largement du contexte financier national.

Les preuves issues de travaux d'évaluations sur l'efficacité de ces instruments financiers cofinancés sont minces, et principalement concentrées sur le soutien aux entreprises. Il existe peu d'informations sur les taux de remboursement et de réinvestissement, ou sur le niveau de participation du secteur privé. Cependant, certains éléments indiquent que

les instruments financiers ont contribué aux objectifs des PO, en particulier concernant un meilleur accès au financement, l'une des principales raisons présidant à l'utilisation d'instruments financiers dans les PO FEDER 2007-13. La transférabilité des leçons acquises sur les domaines où les instruments financiers sont les plus efficaces est limitée par les spécificités contextuelles de leur mise en œuvre : les retours d'évaluations suggèrent que les instruments financiers sont le plus efficace lorsqu'ils sont ajustés à des circonstances nationales ou régionales spécifiques, et donc qu'il n'existe pas de format unique approprié. Les modèles de mise en œuvre sont rarement transférables sans modification prenant en compte les éléments circonstanciels locaux, régionaux, ou nationaux. Cela peut inclure des différences en matière de conditions économiques, de systèmes bancaires et légaux, d'expériences passées de la mise en œuvre des instruments financiers etc.

La courbe d'apprentissage de la mise en œuvre des instruments financiers sur plusieurs périodes de programmation fournit des indications sur les conditions qui soutiennent une mise en œuvre des instruments financiers efficace. Les instruments sont le plus efficace :

- Quand ils sont basés une évaluation pertinente de la situation de marché
- Quand il y a de la flexibilité et une capacité à réagir aux changements
- Quand il y a des protections contre une déviation des objectifs initialement fixés
- Quand ils sont construits sur une expérience préalable
- Quand l'aide est bien ciblée et en lien avec la stratégie du programme.

Le recours aux instruments financiers cofinancés par le FEDER, le Fonds de Cohésion, le FSE et le FEAMP en 2014-20

Selon les données indicatives des Programmes Opérationnels (PO), les Etats membres ont prévu de presque doubler le montant alloué aux instruments financiers, de 11,4 milliards d'euros des Fonds Structurels 2007-13 à environ 21 milliards d'euros en 2014-20. Les prévisions varient sensiblement, avec quatre Etats membres prévoyant d'allouer plus de quatre fois les montants de 2007-13 (NL, PT, RO, SI), et d'autres prévoyant de réduire, ou même d'interrompre l'utilisation d'IF. Certains Etats membres envisagent d'allouer plus de 8% des montants de leurs PO sous forme d'instruments financiers (BG, HU, LT, NL, PT, SI, and UK). Néanmoins, dans le cas de plusieurs PO, la conception et la mise en œuvre d'instruments financiers reste en cours d'élaboration, et les résultats finaux sont susceptibles de différer des prévisions des OP de façon significative. Les changements appliqués aux prévisions en terme d'instruments financiers sont aussi influencés par les résultats des évaluations ex-ante.

En 2007-13, l'utilisation des instruments financiers était principalement l'apanage du Fonds Européen de Développement Régional. Tous les Etats membres qui ont eu recours à des instruments financiers ont mobilisé le FEDER pour les cofinancer, dont sept ont également mobilisé le FSE, et six le FEAMP. Le Fonds de Cohésion ne pouvait pas être utilisé sous la forme d'instruments financiers en 2007-13. En 2014-20, les allocations prévues aux instruments financiers proviennent encore essentiellement du FEDER, mais le recours au FSE et au FEAMP a également augmenté – l'augmentation générale de l'utilisation prévue de ressources de l'UE pour les instruments financiers via le FEDER et le FSE est globalement la même (presque doublée).

L'analyse des plans de financements des instruments financiers montre que plus de la moitié des dépenses prévues (52%) sont orientées vers les PME (Objectif Thématique 3). 17% sont alloués d'une part à la recherche et l'innovation (Objectif Thématique 1), et autant à l'économie bas-carbone (Objectif Thématique 4)

Quelques 157 PO FEDER, FSE et Fonds de Cohésion, soit un peu plus de la moitié, ont alloué des fonds aux instruments financiers (sans compter les programmes Interreg, dont aucun ne prévoit d'utiliser des IF). Cependant, l'ordre de grandeur des instruments financiers prévus varie grandement, à la fois en termes absolus et en pourcentage du PO concerné. Quatorze PO ont prévu des dépenses excédant 400 millions d'euros ; ceux-ci représentent en cumulé 55% des dépenses totales prévues sous forme d'instruments financiers. 27 PO prévoient d'allouer plus de 20% de leur enveloppe aux instruments financiers. Seuls 5 PO FEAMP ont arrêté un plan définitif d'utilisation d'instruments financiers en 2014-20, pour lesquels 80 millions d'euros ont été réservés. En outre, six Etats membres ont mis en œuvre ou prévoient de mettre en œuvre des PO pour l'Initiative PME (BG, ES, IT, FI, MT and RO).

L'avancement de la mise en œuvre varie également nettement entre et au sein de chaque pays. Plusieurs Etats membres sont toujours engagés dans des stades primaires de mise en œuvre (bien que cet état de fait soit constamment en mouvement et en progrès). Un nombre significatif d'évaluations ex-ante sont achevées (143 au moment de l'écriture de ce rapport). Les approches choisies par celles-ci sont multiples, avec certaines Autorités de Gestion organisant les évaluations ex-ante en blocs, ou en étapes, pendant que d'autres entreprenaient des mises à jour d'études existantes. De plus, des évaluations ex-ante ont été réalisées à l'échelle des Fonds (par exemple, pour le FEDER), au sein d'un PO ou travers plusieurs, pour l'ensemble des fonds au sein d'un OP, pour des instruments spécifiques ou des produits financiers déjà envisagés ou pour des Objectifs Thématiques spécifiques. Au moment de l'écriture du présent rapport, peu d'Instruments Financiers étaient opérationnels – ceux développés sur la base d'une expérience préalable, et notamment dans le domaine du soutien aux entreprises.

Les problématiques pratiques, légales et administratives liées à l'utilisation des instruments financiers cofinancés par les fonds.

Selon les recherches menées dans le cadre de la présente étude, l'appréciation par les Autorités de Gestion des avantages et inconvénients des différentes formes de soutien (subventions vs. instruments financiers) n'est pas prioritairement conçue en termes de pour et contre, mais plutôt en termes de type de projets approprié. A différentes formes de soutien correspondent différents types de projets – les AG considèrent le développement des PME (OT3), l'économie bas-carbone (OT4), et la recherche et l'innovation (OT1) comme les domaines les plus adaptés aux instruments financiers.

Le principal inconvénient des subventions, selon les AG, consiste en leur manque de soutenabilité, et le risque qu'elles comportent de créer une 'culture de la subvention', tandis que le principal inconvénient des instruments financiers réside dans leur complexité administrative. Les IF sont considérés par les AG comme plus complexes à administrer que les subventions, en raison d'un manque d'expérience, de la qualité du cadre réglementaire, et de la charge administrative qui y est associée, bien que les intermédiaires financiers permettent parfois d'en réduire le poids. Certaines AG considèrent par ailleurs que la charge administrative des IF est inférieure à celle des subventions pour les bénéficiaires finaux.

Le terme d'« instrument financier » est devenu un attrape-tout pour toutes les formes de soutien remboursable, à la différence des subventions. En pratique cependant, le terme comprend une variété de formes qui ont parfois peu à voir entre elles. Le choix d'un produit financier par une AG est en premier lieu motivé par le résultat de l'évaluation ex-ante.

La relation entre différentes formes de soutien (subventions, IF, etc) est importante - à moins que les divers instruments soient correctement adaptés aux exigences de la politique menée et du marché, et articulés entre eux, il existe des risques que les mesures mises en œuvre entrent en concurrence, se chevauchent, ou bien laissent des besoins insatisfaits. La concurrence ou le chevauchement entre des formes de financement peut être minimisé grâce à une conception adéquate du programme.

Certaines Autorités de Gestion ne prévoient pas d'utiliser d'IF du tout, alors que d'autres y ont recours, ou prévoient d'y recourir pour certains, voire tous les Objectifs Thématiques. Le sondage des Autorités de Gestion cherchait à comprendre pourquoi les instruments financiers n'avaient pas été mobilisés. Dans l'ensemble, les principales raisons énoncées pour expliquer le non-recours aux IF concernent leur inadéquation avec les projets planifiés (e.g ne générant pas de revenus) ; néanmoins, dans le cadre des OT3 et OT4, où les IF sont le plus utilisé, la principale raison expliquant la non utilisation d'IF concerne un manque de demande anticipée des bénéficiaires finaux.

Dans les règlements pour 2014-20, la Commission a introduit la possibilité pour les AG de recourir à des IF types qui respectent des conditions générales standard (off-the-shelf/prêts à l'emploi). Ces modèles types ont pour but de faciliter la mise en place d'un IF ; si le modèle est appliqué, les AG ont l'assurance de la conformité de l'IF proposé avec un ensemble de dispositions réglementaires, y compris concernant la sélection des intermédiaires financiers, les accords de financement, les règles relatives aux aides d'Etat, et les coûts et frais de gestion. Les opinions concernant les instruments « prêts à l'emploi » sont plutôt positives, mais le recours à ces derniers a été faible, en raison du calendrier de publication de la réglementation et la volonté d'une plus grande flexibilité à l'échelon national et régional. Dans certains cas, les instruments « prêts à l'emploi » ont servi de source d'inspiration dans la conception de produits financiers plus adaptés aux besoins locaux.

Les Règlements 2014-2020 fondant l'utilisation des instruments financiers constituent un changement substantiel par rapport à ceux de la période 2007-13, en partie en réaction aux préoccupations des Etats membres face au manque de précision et de clarté de ces règles lors de la précédente période de programmation. L'impression générale des Autorités de Gestion sur le nouveau cadre réglementaire est plutôt mitigée, bien qu'il faille noter que ce dernier est généralement considéré comme complexe. Certaines Autorités de Gestion avaient un avis positif sur la nouvelle réglementation, et l'obligation de procéder à une évaluation ex ante a été perçue très favorablement ; cela dit, une opinion plus largement partagée soulignait que les Règlements pouvaient être améliorés. Une source de préoccupation importante concerne l'incertitude associée aux marges d'interprétation.

Le cadre réglementaire des instruments financiers en 2014-20 a été caractérisé par un accent considérablement accru porté sur le soutien, notamment via *fi-compass*, ainsi que sur les guidances de la Commission. Néanmoins, un nombre significatif d'Autorités de Gestion estime que plus de guidances sont nécessaires dans certains domaines, et trois sources de difficultés ont été identifiées :

- Timing : il y a souvent eu un délai significatif entre la publication de la réglementation et la disponibilité des guidances
- Adaptation : plusieurs AG trouvent les guidances trop générales par rapport à leurs besoins, et souvent trop théoriques, ou bien manquant d'exemples pratiques, et souhaiteraient davantage de contacts directs et efficaces avec la Commission en lien avec des besoins spécifiques.
- Statut : l'impact que les guidances peuvent avoir sur les audits, et l'impression que la Commission applique parfois des règles plus strictes dans les guidances que celles induites par les règlements eux-mêmes.

En considérant quels amendements au cadre règlementaire pourrait faciliter l'utilisation des Instruments Financiers, les facteurs identifiés incluent des changements apportés aux règles relatives aux aides d'Etat, de la simplification, une meilleure communication de la Commission, de la formation, de l'information et du conseil.

L'articulation entre les instruments financiers du FEDER, du Fonds de Cohésion, du FSE et du FEAMP et le FEIS

Les Fonds ESI font partie d'un paysage complexe de mécanismes de financement, privés et publics, domestiques et cofinancés par l'UE, visant les niveaux national, régional et européen. Les AG peuvent allouer des ressources FESI à des instruments conjoints tels que l'Initiative PME, et également rechercher des complémentarités avec d'autres instruments gérés directement au niveau européen (souvent administrés par le Groupe BEI). Le Règlement Portant Dispositions Communes (RPDC) fait explicitement référence à la possibilité d'engager des ressources (FEDER et FEADER) dans l'Initiative PME. Cela permet aux AG d'allouer des ressources à des Instruments Financiers établis au niveau UE. Jusqu'à présent, l'utilisation de l'Initiative a été plutôt limitée ; seules la Bulgarie, la Finlande, l'Italie, Malte, l'Espagne et la Roumanie s'y sont engagées. Une partie de l'explication de cette utilisation limitée provient de changements contextuels : le mécanisme a été introduit pour répondre à des problèmes de liquidité dans le secteur bancaire qui se sont avérés moins sévères que prévu.

Il existe un ensemble plus large d'instruments financiers européens faisant l'objet d'une gestion centralisée qui présentent potentiellement d'importantes synergies avec les activités couvertes par la politique de Cohésion, notamment COSME, qui vise à améliorer l'accès au financement des PME via des prêts, des garanties, et des investissements en fonds propres ; InnovFin, les instruments Horizon 2020 de partage des risques et de financement partagé à destination des PME innovantes ; et le Mécanisme pour l'Interconnexion en Europe (MIE), qui apporte des financements aux projets énergétiques, de transports, et digitaux. Une autre nouveauté au niveau européen est l'introduction du Fonds Européen pour les Investissements Stratégiques (FEIS), établi par la Commission Européenne et la Banque Européenne d'Investissement comme la pierre angulaire du nouveau Plan d'Investissement pour l'Europe. La Commission a publié en Avril 2016 une guidance pour assurer la coordination, les synergies et complémentarités entre les FESI et le FEIS.

La relation entre les instruments financiers des Fonds ESI et les autres instruments européens de différentes natures n'est pas bien comprise par les AG, bien que les AG soient plus en mesure de formuler une opinion à propos de l'articulation entre les IF FESI et les autres instruments lorsque les évaluations ex ante sont achevées. Ces AG sont plus susceptibles de percevoir une concurrence entre les IF FESI et les autres instruments que les AG qui n'ont pas mené d'évaluation ex ante. Par ailleurs la relation entre les IF FESI et les autres sources de financement UE est vectrice de préoccupations. Cela concerne particulièrement la compétitivité des IF FESI et la perception que ces derniers sont désavantagés par rapport aux autres sources de financement UE à cause des règles relatives aux aides d'Etat, et dans une certaine mesure, des difficultés liées aux règles de marché public. Les intermédiaires financiers ont en général eu une approche plus exhaustive concernant les sources de financement, mais ont également perçu un paysage encombré et confus. Il existe par ailleurs des possibilités de chevauchement entre les instruments financiers des FESI et ceux soutenus par le FEIS, et tandis que certains y voient des opportunités de synergies, la plupart y voit une source importante de difficultés.

Conclusions et recommandations

L'objectif de la section finale du rapport est de fournir des conclusions sur les forces et faiblesses du cadre réglementaire établi au niveau européen concernant l'utilisation d'instruments financiers, et d'identifier des recommandations spécifiques pour de potentielles améliorations et options pour le futur en termes de réglementation, et de recours aux instruments financiers cofinancés par le FEDER, le Fonds de Cohésion, le FSE et le FEAMP.

Les recommandations émergeant de l'étude sont essentiellement de trois natures :

Premièrement, il existe un besoin de réévaluer le rôle des Instruments Financiers de la politique de Cohésion à la lumière d'un environnement d'intervention de plus en plus complexe. Les Instruments Financiers de la politique de Cohésion présentent des forces spécifiques, telles que leur capacité à s'adapter aux conditions régionales, ou à accompagner le développement de marchés financiers locaux, mais les dispositions réglementaires des IF de la politique de Cohésion s'avèrent coûteux par rapport à plusieurs initiatives horizontales ou au niveau européen, et alors que les synergies entre différentes initiatives sont devenues le Saint Graal de la mise en œuvre des politiques publiques, leur réalisation nécessite d'importantes capacités administratives.

Deuxièmement, il apparait essentiel d'augmenter le niveau de stabilité de la régulation. Dans le cadre des cycles 2007-13 et 2014-20, les discussions au sujet de l'efficacité des instruments financiers ont été dominées par les difficultés liées aux modalités de mise en conformité et aux procédures, plus que par des questions de conception de la politique, de focus sur « ce qui marche et dans quelles circonstances », afin de remplir les objectifs spécifiques en matière de développement économique.

Enfin, dans la continuité des points développés précédemment, il existe des éléments en faveur d'une réorientation des guidances. Le soutien accru apporté a été largement apprécié, mais les Autorités de Gestion se sont montrées critiques au sujet de leur timing, ainsi que de leur statut par rapport aux exigences de l'audit. Plus spécifiquement, si les IF deviennent de plus en plus largement utilisés dans des domaines où l'expérience est limitée, un soutien plus ajusté et un partage de bonnes pratiques sont nécessaires.

L'idée directrice des recommandations présentées ci-dessus est la consolidation, la coordination et la stabilisation du cadre réglementaire appliqué aux instruments financiers, et le soutien au développement des capacités administratives au sein des Autorités de Gestion. Bien entendu, il est également possible de soutenir des options plus radicales en faveur d'un plus grand usage et une plus grande efficacité des instruments financiers. Ces dernières incluent la limitation de la mise en œuvre des IF dits « prêts à l'emploi », l'obligation de recourir à des instruments établis au niveau européen, la réservation d'une partie de l'enveloppe des programmes opérationnels aux IF, l'utilisation des seules subventions dans le domaine de la gestion partagée, ou l'imposition d'une utilisation par défaut d'un IF, accompagnée d'une obligation de justifier explicitement l'utilisation de subventions en faveur des investissements productifs. En pratique, la méthode d'avancement la plus efficace est susceptible de comprendre une combinaison d'éléments inclus dans ces options, et une approche plus nuancée prenant en compte les expériences passées. En d'autres termes, une approche incrémentale du changement de politique publique et le soutien à l'utilisation d'IF – en bâtissant sur l'expérience, l'apprentissage, et le développement de capacités administratives, mais en opérant des ajustements de politique afin de maximiser les bénéfices liés aux éléments qui ont bien fonctionné, ou pourrait bien fonctionner. Le recours aux IF cofinancés a donné lieu au développement de capacités administratives et de réseaux politiques nécessaires pour faciliter leur utilisation. La stabilité réglementaire est essentielle pour consolider cette expérience et permettre de recentrer les attentions sur les *changements substantiels* que les IF peuvent générer, plutôt que les *difficultés procédurales*. Pour cela, plus et mieux d'informations est nécessaire, pour permettre une analyse fine sur les produits financiers cofinancés qui fonctionnent et comprendre comment : les preuves concrètes concernant comment et où les IF peuvent être efficaces, de mêmes que les modèles de « réussite » pourraient fournir des raisons convaincantes pour augmenter leur utilisation.

Zusammenfassung

ESI-Fonds und Finanzinstrument: Hintergründe

Zur Zeit der Planung und der ersten Umsetzung der EU-Kohäsionspolitik 2014-20 waren die Nachwirkungen der schwersten Finanzkrise seit den 1930er Jahren noch zu spüren. Die Auswirkungen der Krise haben sich als sowohl weitreichend als auch langanhaltend erwiesen und Europa erholt sich im Allgemeinen nur langsam. Ein entscheidender Faktor für die schwache Erholung sind die Auswirkungen der Krise auf sowohl öffentliche als auch private Investitionen, trotz der historisch niedrigen Zinssätze und dem hohen Maß an Liquidität auf den europäischen Kapitalmärkten. Die wichtigsten Gründe sind die Unsicherheit und die systemisch niedrige Wirtschaftsaktivität. Im Allgemeinen gibt es mittlerweile zwar keine Schwierigkeiten mehr beim Zugang zu Finanzmitteln, Anlass zu ernsthaften Bedenken gibt es aber weiterhin für bestimmte Marktsegmente, vor allem für KMUs und Infrastruktur.

Sowohl private als auch öffentliche Quellen spielen eine wichtige Rolle bei der Bereitstellung von Finanzmitteln, allerdings ist deren Unterscheidung nicht immer ganz einfach. In vielen EU-Mitgliedsstaaten ist der öffentliche Sektor seit längerem an der Bereitstellung von Finanzinstrumenten (FI) zur Verfolgung entwicklungspolitischer Ziele beteiligt. Im Rahmen der Finanzkrise nahmen nationale Förderbanken eine stärkere Rolle ein und diese gewinnen auch weiterhin an Bedeutung. Nationale Förderbanken können FI direkt zur Verfügung stellen, agieren meistens aber auf indirekte Weise, oft über Geschäftsbanken. EU-Finanzquellen werden ebenfalls zunehmend über diese nationalen Quellen gelenkt.

Die Rechtfertigung für eine öffentliche Intervention in die Wirtschaftsförderungspolitik besteht darin, Tätigkeiten zu unterstützen, die die Marktteilnehmer nicht allein leisten können oder wollen, von denen man aber annimmt, sie seien im öffentlichen Interesse. Dies wird manchmal als „Marktversagen" bezeichnet, kann aber auftreten wenn es einfach keinen Markt gibt und der private Sektor durchaus rational operiert oder wenn der Markt mangelhaft ist und suboptimal operiert. Dies ist der Fall bei der Bereitstellung öffentlicher Güter, der Versorgung mit meritorischen Gütern, der Präsenz von Externalitäten und bei mangelhafter Information auf den Finanzmärkten. Nicht alle diese Marktunvollkommenheiten können mit FI angesprochen werden.

FI bieten einige Vorteile gegenüber nicht rückzahlbaren Instrumenten (so zum Beispiel Nachhaltigkeit und Kosteneffizienz), müssen aber an die jeweiligen Umstände angepasst werden und können letztendlich nur eingesetzt werden, wenn die Investitionen einkommenserzeugend sind, so dass die anfängliche Unterstützung zurückgezahlt werden kann. Bei der Betrachtung von Formen der Intervention und der Grundprinzipien von FI ist es wichtig zu erwähnen, dass der Begriff „Finanzinstrument" sehr unterschiedliche Finanzprodukte abdeckt. Diese unterscheiden sich stark, was ihre Eignung für unterschiedliche Zielsetzungen, die Implikationen für Empfänger und ihre Art der Steuerung anbelangt.

Was die Gründe für eine Nutzung von kofinanzierten Instrumenten in der Kohäsionspolitik anbelangt, so ist anzumerken, dass diese vor allem kontextbestimmt sind. Sie spiegeln das Ausmaß und den Fokus von OPs wieder, den Grad an Experimentierfreude mit in der nationalen Politik wenig genutzten Formen der Finanzierung, sowie die weiteren staatlichen Finanzzusammenhänge wieder.

Evaluierungsbelege für die Effektivität von kofinanzierten FI gibt es wenige und sie konzentrieren sich auf kofinanzierte FI zur Unternehmensunterstützung; es gibt wenig Beweise für revolvierende Effekte oder das Ausmaß der Beteiligung des privaten Sektors. Es gibt jedoch Belege dafür, dass FI zur Erreichung der Zielsetzungen von OPs beigetragen haben, insbesondere durch einen verbesserten Zugang zu Finanzmitteln – einer der wichtigsten Gründe für den Einsatz von FI in den EFRE OPs 2007-13. Die Übertragbarkeit von Lehren zum effektiven Einsatz von FI wird beschränkt durch den kontextspezifischen Charakter der FI-Implementierung: Es gibt Hinweise, dass FI dann am effektivsten sind, wenn sie auf spezifische regionale oder nationale Umstände zugeschnitten sind, da es keinen erfolgreichen einheitlichen Ansatz gibt. Modelle sind nur selten übertragbar ohne Abänderungen zur Berücksichtigung lokaler, regionaler oder nationaler Umstände. Dazu gehören Unterschiede bei lokalen wirtschaftlichen Rahmenbedingungen, sowie bei Bank- und Rechtssystemen und vorherige Erfahrungen bei der Umsetzung von FI etc.

Die Erfahrungskurve bei der Implementierung von FI über mehrere Programmperioden liefert Anzeichen für die Bedingungen zur Unterstützung einer effektiven FI-Umsetzung. FI sind am effektivsten:

- wenn sie auf einer akkuraten Einschätzung der Marktsituation basieren,
- wenn sie Flexibilität bieten, sowie die Fähigkeit auf Veränderungen zu reagieren,
- wenn es eine Absicherung vor einer Verlagerung von Zielsetzungen gibt,
- wenn sie auf vorherigen Erfahrungen aufbauen, und
- wenn die Förderung fokussiert ist und in Verbindung zur Programmstrategie steht.

Der Einsatz von Finanzinstrumenten, die über EFRE, Kohäsionsfond, ESF und EMFF für 2014-20 kofinanziert werden

Laut indikativer Angaben in den Operationellen Programmen (OPs) planten Mitgliedsstaaten ihre Ausgaben für FI beinahe zu verdoppeln, von rund 11,4 Milliarden Euro Strukturfondressourcen in 2007-13 auf rund 21 Milliarden Euro für 2014-20. Die Pläne unterscheiden sich stark und vier Mitgliedsstaaten (NL, PT, RO, SI) planen, mehr als das Vierfache der 2007-13 eingesetzten Mittel bereitzustellen, während andere eine Reduzierung oder sogar Beendigung des Einsatzes von FI vorsehen. Einige Mitgliedsstaaten planen, mehr als acht Prozent der OP-Beiträge in Form vom FI einzusetzen (BG, HU, LT, NL, PT, SI und UK). In vielen OPs bleiben der Entwurf und die Implementierung von FI jedoch in einem ständigen Fluss und es ist sehr wahrscheinlich, dass die endgültigen Ergebnisse deutlich von den OP-Plänen abweichen werden. Zudem beeinflussen die Ergebnisse der Ex-ante-Bewertungen eventuelle Änderungen bei der FI-Planung.

2007-13 war der Einsatz von FI vor allem die Domäne des EFRE. Alle Mitgliedsstaaten, die FI einsetzten, nutzten den EFRE zur Kofinanzierung, sieben von ihnen nutzten zudem den ESF. Sechs Mitgliedsstaaten nutzten den EMFF für FI. Der Kohäsionsfonds konnte 2007-13 nicht für FI genutzt werden. Für 2014-20 fällt die geplante FI-Zuweisung vor allem unter den EFRE, aber der Einsatz des ESF und des EMFF hat ebenfalls zugenommen – der gesamte Anstieg beim geplanten Einsatz von EU-Ressourcen für FI im Rahmen des EFRE und des ESF ist in etwa gleich (nahezu das Doppelte).

Eine Analyse der Investitionspläne für FI zeigt, dass mehr als die Hälfte der geplanten FI-Ausgaben (52 Prozent) auf KMUs ausgerichtet ist (Thematisches Ziel 3). Weitere 17 Prozent gehen jeweils an die Bereiche Forschung und Entwicklung (Thematisches Ziel 1) und CO2-Reduktion (Thematisches Ziel 4). Dies bedeutet, dass rund 87 Prozent der gesamten FI-Ausgaben für diese drei Ziele vorgesehen sind.

157 aller EFRE-, ESF- und Kohäsionsfonds-OPs – knapp über die Hälfte – stellen Fördermittel für FI zur Verfügung (mit Ausnahme von Interreg, dessen OPs keinen Einsatz von FI vorsehen). Das Ausmaß der vorgesehenen FI ist jedoch stark unterschiedlich, sowohl absolut, als hinsichtlich ihrer Bedeutung innerhalb des OPs. Vier OPs sehen Ausgaben von mehr als 400 Millionen Euro vor; gemeinsam machen diese 55 Prozent der vorgesehenen FI-Ausgaben aus. 27 OPs planen mehr als 20 Prozent ihrer

Ressourcen für FI einzusetzen. Nur fünf EMFF OPs haben konkrete FI-Pläne für 2014-20, für die rund 80 Millionen Euro vorgesehen sind. Zusätzlich haben oder planen sechs Mitgliedsstaaten OPs im Kontext der KMU-Initiative (BG, ES, IT, FI, MT und RO).

Fortschritte bei der Implementierung von FI variieren innerhalb und zwischen Ländern. Viele Mitgliedsstaaten befinden sich noch immer in einer frühen Phase der FI-Implementierung, wobei sich die Situation jedoch ständig verändert. Eine bedeutende Zahl an Ex-ante-Bewertungen wurde abgeschlossen (zum Zeitpunkt der Verfassung dieses Berichts geschätzte 143). Die Ansätze waren hierbei sehr unterschiedlich. Einige Verwaltungsbehörden haben Ex-ante-Bewertungen in Blöcken oder Abschnitten durchgeführt, andere haben existierende Studien aktualisiert. Zusätzlich fanden teilweise auch auf Fonds-Ebene Ex-ante-Bewertungen statt (z.B. für EFRE), entweder innerhalb eines OPs oder auf OP-übergreifender Basis, für alle Fonds innerhalb eines OPs, für spezifische Instrumente oder bereits vorgesehene Finanzprodukte oder für spezifische Thematische Ziele. Zum Zeitpunkt der Verfassung dieses Berichts waren nur wenige FI operativ – zumeist jene, die auf vorherigen Erfahrungen basierten und sich mit Unterstützung für Unternehmen befassten.

Praktische, rechtliche und verwaltungstechnische Aspekte beim Einsatz kofinanzierter Finanzinstrumente

Laut der für die Studie durchgeführten Forschungsarbeit bilden sich Verwaltungsbehörden ihre Meinung zu den Vor- und Nachteilen unterschiedlicher Arten der Förderung (Zuschüsse vs. FI) nicht vorrangig auf Basis von Pro- und Kontraüberlegungen, sondern vielmehr auf Basis der Art von Projekten, für die FI sich am besten eignen. Unterschiedliche Arten der Förderung eignen sich für unterschiedliche Arten von Projekten – Verwaltungsbehörden sehen KMU Entwicklung (TZ3), Kohlenstoffarme Wirtschaft (TZ4) und Forschung und Entwicklung (TZ1) als die am besten geeigneten Einsatzbereiche für FI.

In den Augen der Verwaltungsbehörden sind die wichtigsten Nachteile von Zuschüssen ihre mangelnde Nachhaltigkeit und das Risiko der Entstehung einer „Zuschusskultur", während der größte Nachteil von FI deren administrative Komplexität ist. Verwaltungsbehörden sehen die Anwendung von FI auf Grund mangelnder Erfahrung als schwieriger an als die von Zuschüssen, allerdings können Finanzmittler den Verwaltungsaufwand für FI mildern. Einige Verwaltungsbehörden gehen auch davon aus, dass der Verwaltungsaufwand für Empfänger bei FI niedrige ist als bei Zuschüssen.

Das Preis-Leistungs-Verhältnis ist seit einigen Jahren von zunehmender Bedeutung für die öffentliche Politik und hat dazu geführt, dass oft die Rolle von Zuschüssen bei der Förderung der wirtschaftlichen und sozialen Entwicklung in Frage gestellt wird. Die Auffassung, dass FI ein besseres Preis-Leistungs-Verhältnis bieten, weil Beträge zurückgezahlt und reinvestiert werden, ist eines der Hauptargumente der EU-Kommission für ihren Einsatz. Das Preis-Leistungs-Verhältnis ist jedoch kein intrinsischer Bestandteil einer Förderform – gelegentlich bieten Zuschüsse ein besseres Preis-Leistungs-Verhältnis, auf Grund der Verwaltungskosten von FI. Zu den Argumenten für FI gehört auch, dass sie einen höheren wirtschaftlichen Einfluss haben können, nicht nur weil Fördermittel wiederverwertet werden und mehr Projekte unterstützen, sondern auch, weil der Einsatz rückzahlbarer Fördermittel die Qualität eines Projekts verbessern kann. In den Augen der Verwaltungsbehörden wirkt der wirtschaftliche Einfluss von FI auf mehreren Ebenen, teilweise mit geringeren Ausgaben als dies bei Zuschüssen der Fall ist.

Der Begriff „Finanzinstrument" hat sich zu einer umfassenden Bezeichnung für alle Arten rückzahlbarer Fördermittel entwickelt, im Gegensatz zu Zuschüssen. In der Praxis umfasst der Begriff eine Reihe von Förderformen, die unter Umständen wenig miteinander zu tun haben. Die Auswahl von Finanzprodukten durch die

Verwaltungsbehörden wird vor allem durch die Ergebnisse der Ex-ante-Bewertungen bestimmt.

Die Beziehungen zwischen unterschiedlichen Förderformen (Zuschüssen, FI, etc.) spielen eine wichtige Rolle – sind die unterschiedlichen Instrumente nicht auf die Bedürfnisse von Politik und Markt zugeschnitten und aufeinander abgestimmt, besteht das Risiko, dass Maßnahmen miteinander konkurrieren, sich überlappen oder bestimmte Bedürfnisse nicht abdecken. Konkurrenz und Überlappungen zwischen Finanzierungsformen können durch geeignetes Programmdesign minimiert werden.

Einige Verwaltungsbehörden planen keinen Einsatz von FI, wohingegen andere wiederum vorsehen, sie im Rahmen einiger, oder sogar aller, Thematischer Ziele einzusetzen. Die Befragung von Verwaltungsbehörden sollte zu einem besseren Verständnis der Gründe führen, warum FI nicht eingesetzt werden. Der Hauptgrund für die Nichtnutzung von FI war deren Unangemessenheit für geplante Projekte (z.B. nicht-einkommenserzeugend); der Hauptgrund für eine Nichtnutzung von FI im Rahmen von TZ3 und TZ4 war jedoch die Wahrnehmung, dass eine fehlende Nachfrage seitens der Endempfänger bestünde.

Im Rahmen der Verordnungen für 2014-20 führte die EU-Kommission für Verwaltungsbehörden die Option der Nutzung von FI mit standardisierten AGBs ein („von der Stange"). Die Vorlagenmodelle sollen die Einrichtung von FI erleichtern; werden die Vorlagen befolgt, so können sich Verwaltungsbehörden sicher sein, dass die vorgeschlagenen FI einer Reihe rechtlicher Rahmenbedingungen gerecht werden, einschließlich der Auswahl von Finanzmittlern, der Finanzierungsvereinbarungen, der staatlichen Beihilfe und der Kosten und Gebühren für Verwaltung. Diese FI „von der Stange" werden im Allgemeinen sehr positiv eingeschätzt, allerdings zeigt sich nur eine langsame Akzeptanz, auf Grund des Zeitpunkts der Veröffentlichung der Verordnungen und des Wunsches nach einer größeren staatlichen Flexibilität. In einigen Fällen wurden diese Instrumente „von der Stange" als Inspiration für den Entwurf von Produkten genutzt, die besser auf lokale Bedürfnisse abgestimmt sind.

Die Verordnungen für 2014-20 zur Unterstützung des Einsatzes von FI stellen eine wesentliche Veränderung zu den Verordnungen 2007-13 dar, teilweise als Reaktion auf die Bedenken von Mitgliedsstaaten hinsichtlich fehlender Details und einem Mangel an Klarheit. Die allgemeine Auffassung von Verwaltungsbehörden zum neuen Rechtsrahmen ist sehr unterschiedlich, aber man kann sagen, dass er generell als eine Herausforderung gesehen wird. Einige Verwaltungsbehörden sehen die neuen Verordnungen sehr positiv und die obligatorische Ex-ante-Bewertung wird als sehr positiv betrachtet; weiter verbreitet aber ist die Ansicht, dass die Verordnungen verbesserungsfähig sind. Deutliche Bedenken gibt es in etwa hinsichtlich der Unsicherheit, die mit dem Interpretationsspielraum in Verbindung gebracht wird.

Der Rechtsrahmen für FI für 2014-20 zeichnet sich durch eine deutlich stärkere Schwerpunktsetzung auf Unterstützung bei der Umsetzung aus, vor allem über *fi-compass*, sowie auf über von der Kommission herausgegebene schriftliche Leitlinien. Nichtsdestotrotz ist eine deutliche Anzahl an Verwaltungsbehörden der Ansicht, dass es in gewissen Bereichen zusätzlicher Leitlinien bedarf. Es wurden drei Punkte herausgearbeitet:

- Timing: Oft war der zeitliche Abstand zwischen der Veröffentlichung von Verordnungen und der Verfügbarkeit von Leitlinien sehr groß.
- Eignung: Viele Verwaltungsbehörden sehen die Leitlinien als zu allgemein für ihre Bedürfnisse und als zu theoretisch oder durch zu wenige praktische Beispiele untermauert und wünschen sich mehr und effektiveren direkten Kontakt mit der EU-Kommission bezüglich ihrer spezifischen Bedürfnisse.
- Status: Die Auswirkungen, die Leitlinien auf Prüfungsverfahren haben können sind unklar und es wird wahrgenommen, dass die EU-Kommission bei den Leitlinien teilweise strengere Regeln anwendet als in den Verordnungen selbst vorgesehen.

Überlegungen zu Änderungen des Rechtsrahmens, die die Nutzung oder Annahme von FI erleichtern könnten haben Faktoren wie Änderungen der staatlichen Beihilfevorschriften, Vereinfachungen, verbesserte Kommunikation mit der EU-Kommission, Training, Information und Ratschläge identifiziert.

Die Beziehungen zwischen EFRE-, Kohäsionsfonds-, ESF- und EMFF-FI und anderen EU-Instrumenten sowie EFSI

ESI-Fonds sind Teil eines komplexen Angebots an Fördermechanismen, einschließlich privater und öffentlicher, staatlicher und EU-Quellen, auf regionaler, nationaler und EU-Ebene. Verwaltungsbehörden können ESIF-Ressourcen gemeinsamen Instrumenten beisteuern, wie etwa der KMU-Initiative, und viele streben zudem nach einer Komplementarität mit anderen Instrumenten auf EU-Ebene (oft von der EIB-Gruppe verwaltet). Die Verordnung zu gemeinsamen Bestimmungen bezieht sich spezifisch auf die Möglichkeit, der KMU-Initiative (EFRE und ELER) Ressourcen beizusteuern. Dies ermöglicht es Verwaltungsbehörden, Ressourcen für FI auf EU-Ebene zur Verfügung zu stellen. Bisher ist die Annahme der Initiative relativ beschränkt; nur Bulgarien, Finnland, Italien, Malta, Spanien und Rumänien haben sich dazu verpflichtet. Eine teilweise Erklärung für diese eingeschränkte Annahme könnten die kontextuellen Veränderungen sein: die Regelung wurde eingeführt, um die Liquiditätsprobleme von Banken anzugehen, diese haben sich aber als weniger schwerwiegend herausgestellt als angenommen.

Es gibt auch ein umfassenderes Set an zentral verwalteten FI auf EU-Ebene, die potentiell wichtige Synergien mit den Aktivitäten der Kohäsionspolitik aufweisen, einschließlich COSME, dessen Ziel ein verbesserter Fördermittelzugang für KMUs über Kreditbürgschaften und Eigenkapital ist. Andere Beispiele sind InnovFin, die Horizont 2020 Eigenkapital- und Risikoteilungsinstrumente für innovative KMUs und „Connecting Europe", die Finanzmittel für Energie-, Transport- und digitale Projekte zur Verfügung stellt. Eine weitere Entwicklung auf EU-Ebene ist die Einführung des EFSI (Europäischer Fonds für strategische Investitionen), der von der EU-Kommission und der Europäischen Investitionsbank als Eckpfeiler des neuen Investitionsplans für Europa ins Leben gerufen wurde. Die EU-Kommission gab im April 2016 Leitlinien zur Koordinierung und zu Synergien und Komplementarität der beiden Förderquellen heraus.

Der Zusammenhang zwischen FI der ESIF und anderen EU-Instrumenten unterschiedlicher Art wird von Verwaltungsbehörden nicht immer ausreichend verstanden; dort wo Ex-ante-Bewertungen durchgeführt wurden sind Verwaltungsbehörden aber eher in der Lage, sich eine Meinung über Zusammenhang zwischen ESIF-FI und anderen Instrumenten zu bilden. Bei diesen Verwaltungsbehörden ist es wahrscheinlicher, dass die Wahrnehmung einer Konkurrenz zwischen ESIF-FI und anderen Instrumenten besteht, als bei Verwaltungsbehörden, bei denen keine Ex-ante-Bewertungen durchgeführt wurden und es Bedenken zum Zusammenhang zwischen ESIF-FIs und anderen EU-Finanzquellen gibt. Diese beziehen sich vor allem auf die Wettbewerbsfähigkeit von ESIF-FI und die Wahrnehmung, dass diese auf Grund von staatlichen Beihilfevorschriften und zu einem gewissen Maß auch auf Grund von vergaberechtlichen Vorgaben im Vergleich zu anderen EU-Förderquellen benachteiligt sind. Finanzmittler hatten in der Regel umfassendere Ansichten zu von Förderquellen, viele bestätigten aber, dass die Förderlandschaft zu weitreichend und verwirrend ist. Zudem gibt es potentielle Überlappungen zwischen ESIF- und EFSI-unterstützten FI und obwohl hier teilweise Möglichkeiten für Synergien gesehen werden, sehen die Meisten sie als eine große Herausforderung.

Schlussfolgerungen und Empfehlungen

Ziel dieses letzten Abschnitts des Berichts ist die Formulierung von Schlussfolgerungen zu den Stärken und Schwächen des Rechtsrahmens auf EU-Ebene zur Nutzung von FI, sowie die Herausarbeitung spezifischer Empfehlungen für mögliche Verbesserungen und zukünftige Optionen für den Rechtsrahmen und die Nutzung von FI, die mit Mitteln aus EFRE, Kohäsionsfonds, ESF und EMFF kofinanziert werden.

Die Empfehlungen, die sich aus der Studie ergeben, sind dreifacher Art:

Erstens besteht der Bedarf einer Neubewertung der Rolle kohäsionspolitischer FI vor dem Hintergrund einer zunehmend komplexeren Interventionslandschaft. Kohäsionspolitische FI haben spezifische Stärken, wie etwa ihre Kapazitäten, sich regionalen Gegebenheiten anzupassen oder lokale Finanzmärkte zu entwickeln. Die regulativen Aspekte kohäsionspolitischer FI sind jedoch aufwändig im Vergleich mit vielen horizontalen Initiativen und Initiativen auf EU-Ebene. Während sich „Synergien" zwischen verschiedenen Initiativen zwar zum „Heiligen Gral" bei der Umsetzung regionalpolitischer Ziele entwickelt haben, so verlangt ihre Erzielung doch auch nach geeigneten Verwaltungskapazitäten.

Zweitens gibt es überzeugende Argumente für eine stärkere rechtliche Stabilität. Sowohl in der Programmperiode 2007-13, als auch in der Programmperiode 2014-20 wurden Diskussionen zur Effektivität von FI oft von den Themen Einhaltung der Regeln und Implementierungsprozesse dominiert, anstatt von den regionalpolitischen Inhalten und einem Fokus auf „was funktioniert und unter welchen Umständen", um spezifische Ziele der Wirtschaftsentwicklung anzugehen.

Zu guter Letzt und in Verbindung zum Obenstehenden kann argumentiert werden, dass es einer Neuausrichtung der Leitlinien bedarf. Die verstärkte Unterstützung seitens der EU-Ebene wurde sehr geschätzt, Verwaltungsbehörden haben allerdings Kritik geäußert hinsichtlich des Timings und Status von Leitlinien im Hinblick auf Prüfungsvorgaben. Dies bedeutet, dass mehr maßgeschneiderte Unterstützung und ein Austausch zu bewährten Vorgehensweisen nötig ist, sollen FI in Bereichen mit eingeschränkter Erfahrung vermehrt eingesetzt werden.

Die grundlegende Zielrichtung der oben aufgestellten Empfehlungen ist die Konsolidierung, Koordinierung und Stabilisierung des Rechtsrahmens für FI, sowie die Unterstützung und Entwicklung der Verwaltungskapazitäten von Verwaltungsbehörden. Es wäre auch möglich, radikalere Optionen zur Verbesserung der Annahme und Effektivität von FI zu unterstützen. Dazu könnte eine Reduzierung der Implementierung von FI auf sogenannte Modelle „von der Stange" gehören, die Verpflichtung des Einsatzes von FI auf EU-Ebene, die Zweckbindung eines Teils der EU-Mittel oder eine Bevorzugung zu Gunsten von FI, indem eine ausdrückliche Rechtfertigung für den Einsatz von Zuschüssen verlangt wird. In der Praxis ist die wahrscheinlich effektivste Vorgehensweise eine Kombination verschiedener *Elemente* dieser Möglichkeiten, sowie die Anwendung eines stärker differenzierten Ansatzes, der Erfahrungen der Vergangenheit berücksichtigt. In anderen Worten, ein stufenweiser Ansatz zur Änderung politischer Richtlinien und der Förderung der Annahme von FI – aufbauend auf Erfahrung, Lernprozessen und dem Ausbau von Verwaltungskapazitäten, aber mit einer Anpassung politischer Richtlinien zur Maximierung der Vorteile von Elementen, die sich als erfolgreich erwiesen haben oder erweisen könnten. Der Einsatz kofinanzierter FI ging einher mit dem Ausbau von Verwaltungskapazitäten und der politischen Netzwerke, die zur Unterstützung ihres Einsatzes nötig sind. Rechtliche Stabilität ist unverzichtbar für eine Konsolidierung dieser Erfahrungen, sowie wie die Fokussierung auf eine Schwerpunktverlagerung weg von ***verfahrenstechnischen Herausforderungen*** und hin zu den ***substanziellen Veränderungen***, die FI erreichen können. Dazu werden mehr und bessere Informationen benötigt, die eine detaillierte Analyse kofinanzierter Finanzprodukte ermöglichen, d.h. welche Produkte funktionieren und weshalb. Konkrete Belege dafür wie und wo FI effektiv eingesetzt werden können und „Erfolgsmodelle" würden überzeugende Gründe für eine bessere Annahme der Instrumente liefern.

1. INTRODUCTION

This is the Final Report for the study on improving the take up and effectiveness of financial instruments, prepared by the European Policies Research Centre, University of Strathclyde, Glasgow. Following this introduction (Section 1), this report is in five parts.

Section 2 considers ***the rationale for financial instruments in Cohesion policy***, evidence of the effectiveness of Cohesion policy FIs and provides an overview of the wider national and EU supply side. This draws on existing literature, particularly that used for the recent ex ante evaluation of financial instruments under Cohesion policy 2007-13, but also the wider literature sourced by the national expert team for the study.

Section 3 provides a ***'snapshot' of the use of financial instruments in 2014-20***. Among other sources, it uses a combination of Operational Programme data, desk research and an online survey of Managing Authorities to provide an overview of planned use of financial instruments and to establish the extent to which FIs are actually operational.

Section 4 assesses the ***practical, legal and administrative issues*** in the use of financial instruments co-financed by the funds. These focus on a number of aspects, including: the pros and cons of different forms of support; the rationales for the use and non-use of financial instruments; the value of off-the-shelf instruments; the decision-making process for the setting up financial instruments; and the extent to which the legal framework facilitates or hinders the use of financial instruments.

Section 5 examines ***the relationship*** between the ERDF, the Cohesion Fund, the ESF and the EMFF, on the one hand, and the EU level financial instruments, instruments managed by the EIB and EFSI, on the other. This section considers: the extent to which the ERDF, the Cohesion Fund, the ESF and the EMFF overlap and/or compete with commercial or other public FIs; the rationale for and mechanisms through which joint and EU level instruments are used; and the incentives and disincentives for Cohesion policy funded financial instruments as opposed to other FIs.

Section 6 sets out the conclusions from the study on the strengths and weaknesses of the legislative framework for FIs, and offers some options and recommendations for possible improvements regarding the legal framework and the uptake of ESIF co-financed measures.

This report is supported by several **Annexes**:

- Annex 1: Case studies
- Annex 2: Institutions involved in supply of public sector FIs in EU28
- Annex 3: Summary of FIs 2007-13 and 2014-20
- Annex 4: Operational and near-operational FIs – selected examples (Spring 2016)
- Annex 5: Methodological issues

2. RATIONALES FOR FINANCIAL INSTRUMENTS CO-FINANCED BY THE FUNDS

KEY FINDINGS

- ESI Funds have been planned and implemented in the aftermath of the worst financial crisis since the 1930s.
- Private and public investment has yet to recover, in spite of historically low interest rates and high levels of liquidity in European capital markets.
- The underlying issue relates to uncertainty and systemically low rates of economic activity.
- There is no longer a general problem of access to finance, but certain market segments still find this challenging– notably SMEs and infrastructure.
- Private and public sources play an important role in the supply of finance, but are not always easy to distinguish.
- Access to finance for SMEs has improved, but recovery remains fragile and continued uncertainty is affecting investment. Bank loans remain the most popular source of finance, with equity the least popular.
- In many EU Member States, the public sector has long been involved in the supply of FIs to pursue policy goals.
- The role of national promotional banks became more prominent during the economic crisis, and has continued to grow. Promotional banks can provide FIs directly, but most frequently operate indirectly, often through commercial banks.
- EU-level sources of funding are increasingly channelled through these domestic sources, including ESIF, EIB, EIF and EFSI; funding is often 'rebranded' making the overall picture of the supply of FIs less transparent.
- Different types of market imperfection justify public intervention, but not all can be addressed using FIs.
- Financial instruments offer some advantages over non-repayable instruments, but must be tailored to circumstances.
- Use of co-financed instruments in Cohesion policy is heavily influenced by size and focus of OP, and national context.
- Evaluation evidence of effectiveness of co-funded FIs is thin and has focused on co-funded FIs for enterprise support; there is little evidence of a revolving effect or anticipated levels of private sector participation.
- FIs have contributed to increasing access to finance – addressing one of the main rationales for using FIs in 2007-13 ERDF OPs.
- Transferability of lessons on where FIs are most effective is limited by the context-specific nature of FI implementation.
- The learning curve of FI implementation over several programming periods provides some evidence of the conditions which support effective FI implementation.
- The relative efficiency of FIs as opposed to grants is underexplored.

The overall objectives of this section are essentially threefold: first, to provide an overview of the ***wider supply side*** and sources of financial instrument being delivered at national and EU levels; second, to explore the ***economic reasoning for using financial instruments***, having regard to the type of market failures that warrant intervention; and third, to set out the evidence identifying the economic context in which the use of financial instruments (FIs) funded through Cohesion policy have proven ***effective.***

In exploring these issues, it is important to take account of the wider macroeconomic context. The financial turmoil in 2008 and the subsequent sovereign debt crises have had a profound effect on the environment for investment and consequently on the 'real' economy. In spite of historically low interest rates, investment has stagnated for much of the last decade in response to persistent uncertainty and low demand, fuelling concerns at the long-term future of the European economy. This has prompted calls to stimulate public investment in order to increase short-term demand and raise potential output, culminating in the Investment Plan for Europe.[1] The changed macroeconomic climate, and wider policy responses to it, has important implications for the environment in which Cohesion policy operates. Against this background, this part of the report begins with a brief review of the wider investment context, focusing on trends since the financial crisis (Section 2.1). Section 2.2 considers the domestic context for funding investment, including access to finance and the provision of national and subnational sources of finance. Section 2.3 explores the economic rationale for public intervention in the market and the potential role for different kinds of financial instrument to address different types of market imperfection, and the circumstance in which financial instruments might be preferred to grants. Last, Section 2.4 reviews the evidence for the effectiveness of financial instruments and context and criteria that contribute to their success.

2.1. The wider investment context

The planning and early implementation of EU Cohesion policy for 2014-20 took place in the aftermath of the worst financial crisis since the 1930s. The impact of the crisis has been both widespread and long-lasting, though its effects have been far from uniform across the EU. Generally, however, Europe has been slow to recover. While growth rates in the period 2007-11 were similar in the EU and the USA, growth in the States has been much more robust since, though in both economies growth is expected to slow somewhat in 2016 and 2017.

More specifically, over the 5-year period 2007-11, GDP growth across the EU was just 0.6 percent, with rates in subsequent years rising from -0.5 percent in 2012 to 2.0 percent in 2015.[2] For the EU as a whole, the scale of the recovery remains modest, with 2 percent and 1.8 percent GDP growth forecast for 2015 and 2016 respectively, though with very significant differences between countries.[3]

A key factor in the weakness of the recovery has been the ***impact of the crisis on investment*** – both public and private.[4] Significantly, in the EU as a whole, investment[5] accounted for a smaller share of GDP in 2015 than in 2005. Indeed, the proportion declined by about 15 percent - from 22.2 percent of GDP in 2007 to 19.3 percent in 2015 (see Figure 2.1).

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[1] https://ec.europa.eu/priorities/jobs-growth-and-investment/investment-plan_en#actions

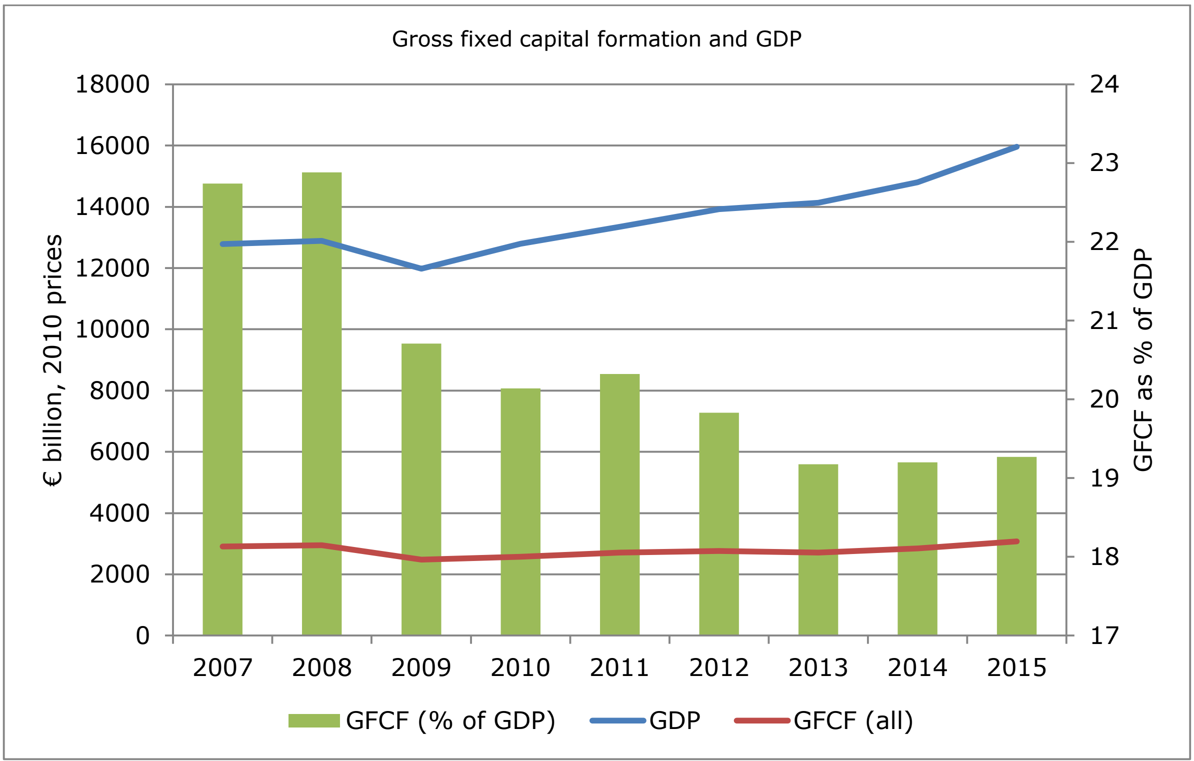
[2] European Commission (2016) Spring economic forecast.

[3] For example, growth rates in 2007-11 ranged from -3.3 percent in the case of Greece to 4.5 percent in the case of Poland; by 2016, all EU economies except Greece (-0.3 percent) are forecast to expand, albeit at differing rates – from Ireland at a forecast 4.9 percent to Finland at just 0.7 percent.

[4] European Commission (2014) European Economic Forecast, Autumn 2014; European Investment Bank (2013) Investment and Investment Finance in Europe; McKinsey & Company (2012) Investing in Growth: Europe's Next Challenge.

[5] As measured by gross fixed capital formation.

Figure 2.1: EU trends in investment (public and private) and GDP



Source: EPRC calculations from AMECO data.

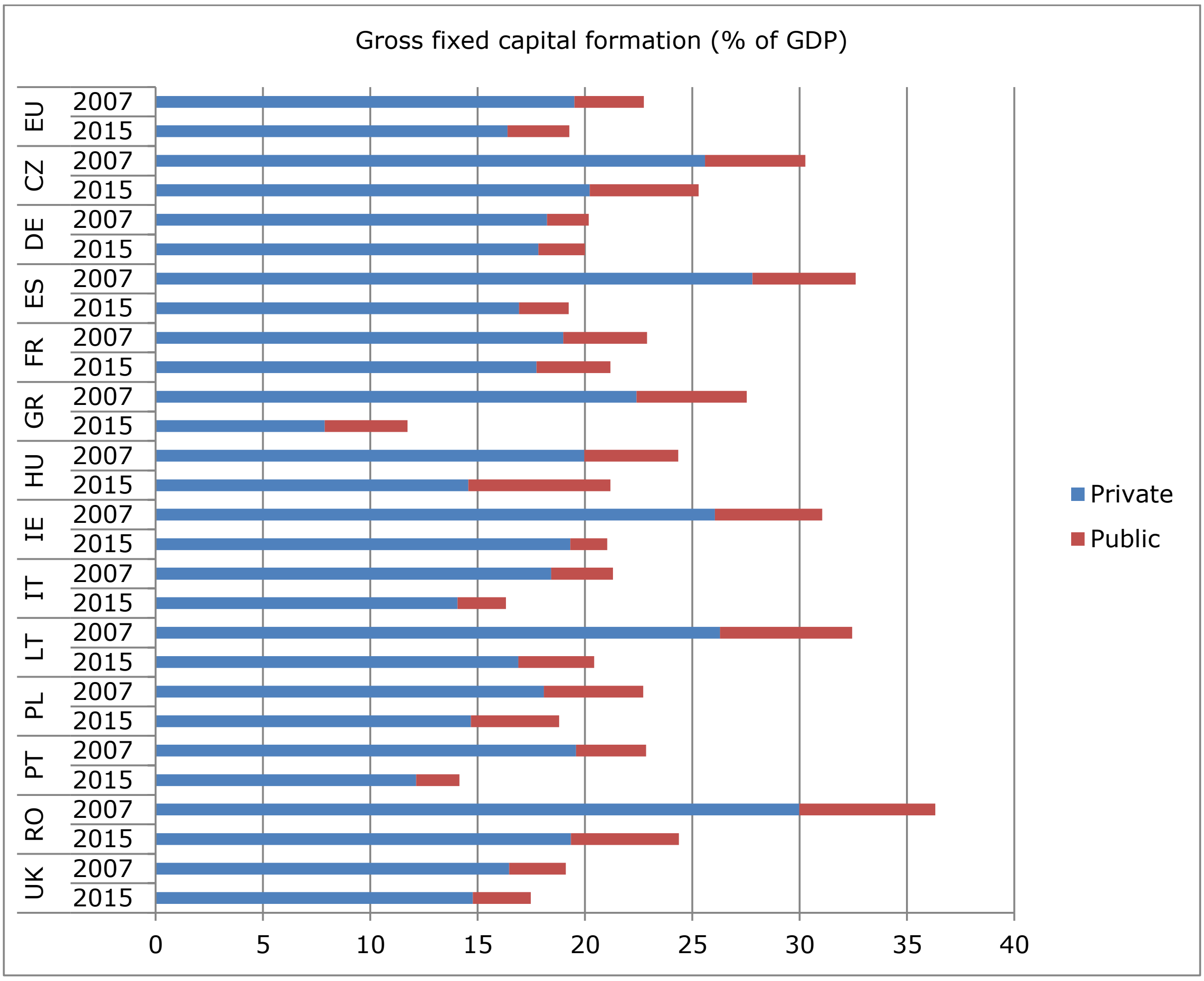
Importantly, the aggregates shown in Figure 2.1 conceal ***significant differences between countries in the contribution of investment to GDP***. These differences apply both to the initial position in terms of the contribution of investment to GDP in 2007, and to the patterns of changes over the period to 2015.

In 2007, the ***contribution of investment to GDP was over 30 percent in some countries*** (Czech Republic, Estonia, Ireland, Latvia, Lithuania, Romania and Spain), but ***less than 22 percent in others*** (Germany, Italy, Luxembourg, the Netherlands and the United Kingdom).

There are also ***distinct patterns of change*** in the contribution of investment to GDP (see also Figure 2.2 for selected countries):

- In some Member States the contribution of investment to GDP was ***broadly the same*** by 2015 as it had been in 2007 - Austria, Belgium, Germany, Malta, Sweden.
- In others, the contribution of investment to GDP ***declined very significantly***: in Greece, Cyprus, Latvia, Spain and Estonia, the decline exceeded 40 percent.

Figure 2.2: Contribution of investment to GDP 2007-2015 (selected countries)



Source: EPRC calculations from AMECO data.

Across the EU, the ***contribution of public investment to GDP*** was around 3.2 percent in 2007 (compared to about 19.5 percent for private fixed capital investment). However, these averages conceal very significant differences between countries. In 2007, ***government investment contributed less than 3 percent of GDP*** in some countries (Austria, Belgium, Germany, Italy and the United Kingdom), but ***more than 6 percent in others*** (Croatia, Estonia, Latvia, Lithuania and Romania).

In looking at ***change in public investment over time***, there are very marked differences between countries. In absolute terms (see Figure 2.3):

- Some countries have experienced a ***dramatic shrinkage in public investment***, notably in Ireland, Spain and Greece where in real terms public investment in 2013-15 was at less than half of 2007-9 levels. These countries had comparatively high levels of public investment, partly related to a pre-crisis boom, and experienced severe cuts as a consequence of the need for fiscal consolidation.
- At the opposite end of the spectrum, other Member States have seen a ***significant increase*** in public investment, most notably in Hungary, Slovakia and Malta – likely partly as a consequence of the impact of Cohesion policy receipts.

Figure 2.3: Changes in public investment 2007-9 and 2013-15

MS	GFCF in 2013-15 as % of 2007-9	MS	GFCF in 2013-15 as % of 2007-9
IE	41.1	**FR**	107.3
ES	42.3	**PL**	107.5
GR	49.4	**SI**	112.7
HR	51.2	**UK**	117.6
CY	53.4	**AT**	119.6
PT	56.0	**EE**	122.2
IT	81.3	**BG**	131.3
LT	87.9	**DE**	131.7
LV	91.9	**FI**	133.1
CZ	92.4	**LU**	134.9
NL	94.6	**BE**	136.9
RO	96.2	**DK**	142.0
EU	99.7	**SE**	154.7
		HU	159.5
		SK	167.8
		MT	218.8

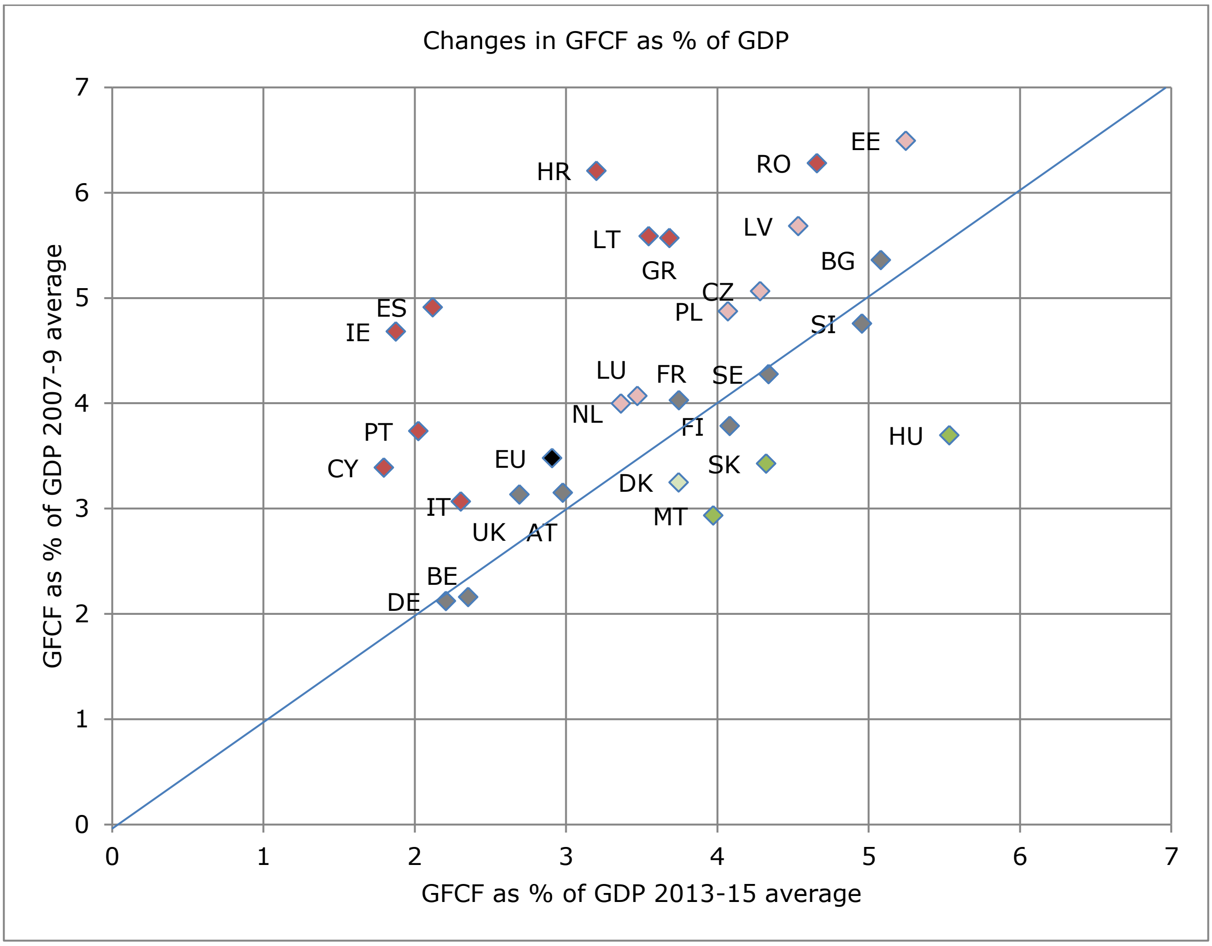
Source: EPRC calculations from AMECO data.

This is broadly reflected in the contribution of public investment to GDP, as illustrated in Figure 2.4. This compares the contribution of public investment to GDP in the period 2007-9 and 2013-15.

At the level of the EU, this contribution fell from 3.5 percent of GDP in 2007-9 to 2.9 percent in 2013-5, a reduction of 16.5 percent. However, ***in several countries, the contribution of public investment to GDP fell by more than 45 percent*** between the two periods (Cyprus, Croatia, Ireland and Portugal). The fall in Greece (34 percent) was less dramatic owing to the sharper and sustained fall in GDP. ***In a few countries, the contribution of public investment to GDP increased by more than 25 percent*** (Hungary, Malta and Slovenia).

In short, the need for fiscal consolidation in a number of EU countries – notably Ireland, Spain, Greece and Portugal, as well as some of the newer Member States – has limited the scope for investment, with implications for private investment and economic activity more generally.

Figure 2.4: Changes in the contribution of public investment to GDP (2007-9 and 2013-15)



Source: EPRC calculations from AMECO data.

Levels of public investment are significantly smaller than private investment in their contribution to GDP (about 3 percent in 2015, compared to about 16 percent), and have different effects on growth and economic activity, but reductions in the level of *private* investment can partly be attributed to reduced *public* investment.[6] Indeed, sustained levels of low public investment may lead to a deterioration of public capital and reduce output in the longer-term,[7] hence IMF arguments in favour of stimulating public infrastructure investment.[8]

Figure 2.5 shows that, for the EU as a whole, ***private investment in 2015 had scarcely regained 2007 levels***, whilst in the US investment was running at over 180 percent of 2007 levels by 2015.

Within the EU figure, patterns of private investment since the crisis vary widely. In 15 Member States, private investment in 2015 had not yet reached 2007 levels in real terms. The situation is particularly acute in Greece where investment in 2015 had declined to less than 30 percent of 2007 levels, while in Spain and Portugal investment in 2015 was at around two-thirds of 2007 levels.

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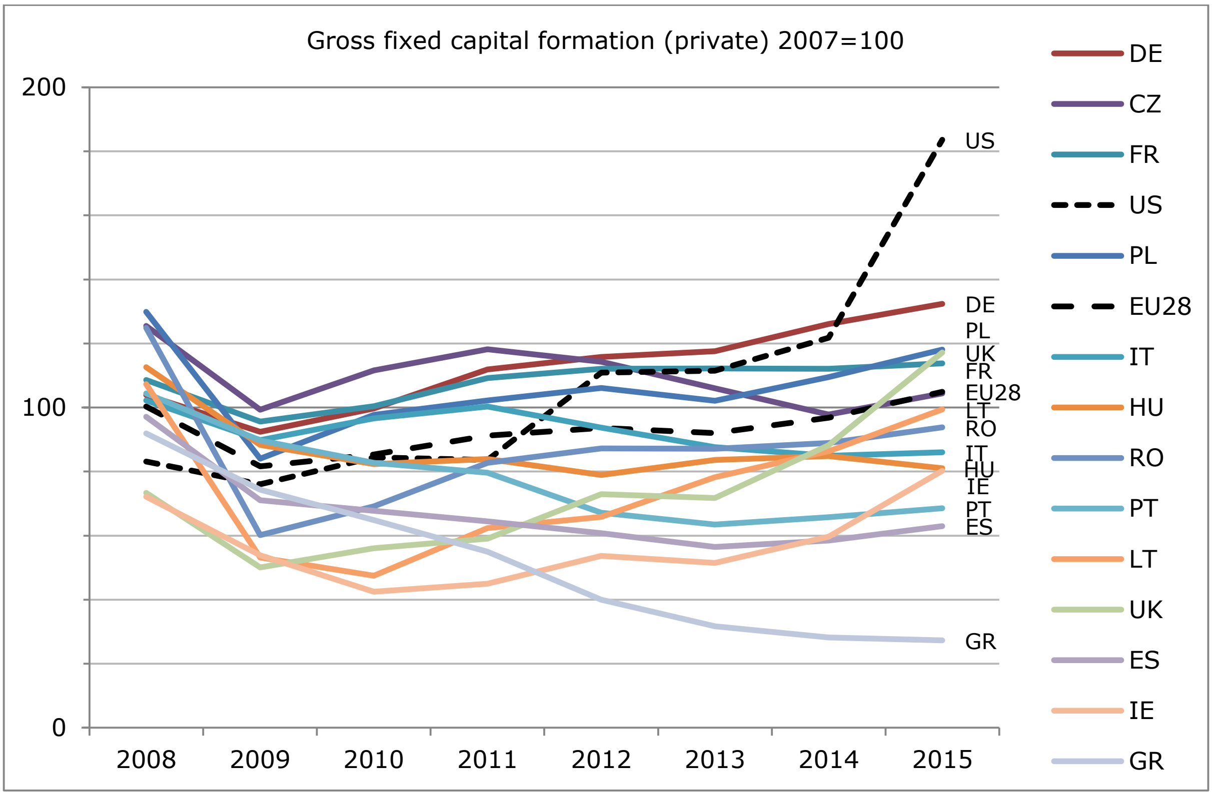
[6] Buti, M. and Mohl, P. (2014) Lacklustre investment in the Eurozone: Is there a puzzle?

[7] ECB (2016) Public Investment in Europe, ECB Economic Bulletin, Issue 2.

[8] IMF (2014) 'Is it time for infrastructure push? The macroeconomic effects of public investment', World Economic Outlook, October.

Figure 2.5: Trends in private investment and the impact of the crisis (selected countries)



Source: EPRC calculations from AMECO data.

Analysis by the European Investment Bank[9] suggests that the prime cause of the collapse and stagnation in private investment is ***uncertainty*** - about the world economy and the longer term implications of the European financial and sovereign debt crisis. Similarly, the IMF has argued that the main factor holding back business investment since the global financial crisis has been the overall weakness of economic activity and firms have reacted to weak sales by reducing capital spending. Other factors, including financial constraints and policy uncertainty, have also held back investment in some economies and some market segments.[10] However, there is a consensus in the IMF and EIB that there is ***no generalised problem of access to finance*** in Europe. In fact, for some activities the reverse is true - firms have increased savings through cost-cutting and lower interest and dividend payments; they have had access to funds, but instead of investing, firms have become savers. Indeed, McKinsey has estimated that listed European companies had excess cash holdings of €750 billion in 2011 – more than double the drop in private investment between 2007 and 2011.[11]

That said, while the supply of finance is not the main problem underlying weak investment, access to finance remains a serious concern for some firms and activities. In this context, the EIB analysis makes clear that ***small and medium-sized and innovative firms*** remain affected by financing constraints, partly owing to their reliance on bank lending, which became curtailed as banks rebuilt their balance sheets and took more cautious approaches to risk. Moreover, the EIB points to significant ***infrastructure*** needs across Europe, with significant challenges for financing as bond markets have

[9] EIB (2013) Investment and Investment Finance in Europe.

[10] IMF (2015) World Economic Outlook

[11] McKinsey & Company (2012) Investing in growth: Europe's next challenge.

dried up and private long-term financing has become more difficult to secure. Furthermore, the Commission points to the significant needs for investments to realise the Energy Union objectives[12] for 2020 and 2030. Similarly, the IMF makes a case for increased public infrastructure investment in economies with clearly identified needs and efficient public investment processes. In this context, additional public infrastructure investment may be warranted to spur demand in the short term, raise potential output in the medium term, and thus "crowd in" private investment. Against this background, the Investment Plan for Europe aims to tap into the high levels of liquidity in Europe's capital markets by sharing risk in order to lever in private investment.

2.2. Access to finance - the provision of finance from private and public sources

This section provides a brief overview of the current status of the provision of finance for enterprises and projects from both private and public sector sources in the EU. It is worth noting that it is becoming increasingly difficult to differentiate between private and public sources of funding. Funds that originate from the public sector (both EU and domestic) are often delivered by commercial banks and private sector fund managers. There is often a lack of transparency over the original source of funding e.g. due to re-branding. Governments also frequently participate in the capital of so-called private banks, which may in fact be majority-owned by the private sector. The status of financial institutions may also change over time (see, for example, the recently privatised Green Investment Bank in the UK).

2.2.1. Private sector sources of finance

While the general economic environment in terms of ***market conditions and access to finance continue to improve***, recovery remains somewhat fragile.[13] Growth estimates have been revised downwards and 'Brexit' contributes to ongoing uncertainty, and is expected to have a negative impact on the recovery process.

Although the SME business climate has improved, continued uncertainty has had an impact on investment decisions. However, in 2014, for the second year in a row, the ***most pressing problem identified by EU28 SMEs was finding customers.*** Access to finance was rated by SMEs on average as the fifth most pressing problem– down from second in 2013. However, 14 percent of SMEs identified access to finance as the most pressing problem they faced, especially those located in Cyprus, Greece and Slovenia.

Among SMEs in EU28 expecting to grow in the next two to three years, ***bank loans were the most preferred type of external financing*** in 2014. The second most preferred type of funding were other sources such as trade credit or loans from related companies, shareholders or public sources. Equity investment was the least preferred type of funding among SMEs with the ambition to grow. In all countries, making existing public measures easier to obtain finance or tax incentives was indicated as the most important driver for improving access to future financing, except in Sweden and the Czech Republic, where SMEs perceived the most important drivers to be making existing public measures easier to obtain finance and the provision of guaranteed loans.

The SAFE survey found that bank loans, bank overdrafts, credit lines or credit card overdrafts and trade credit are used by over 90 percent of EU28 SMEs for which this type

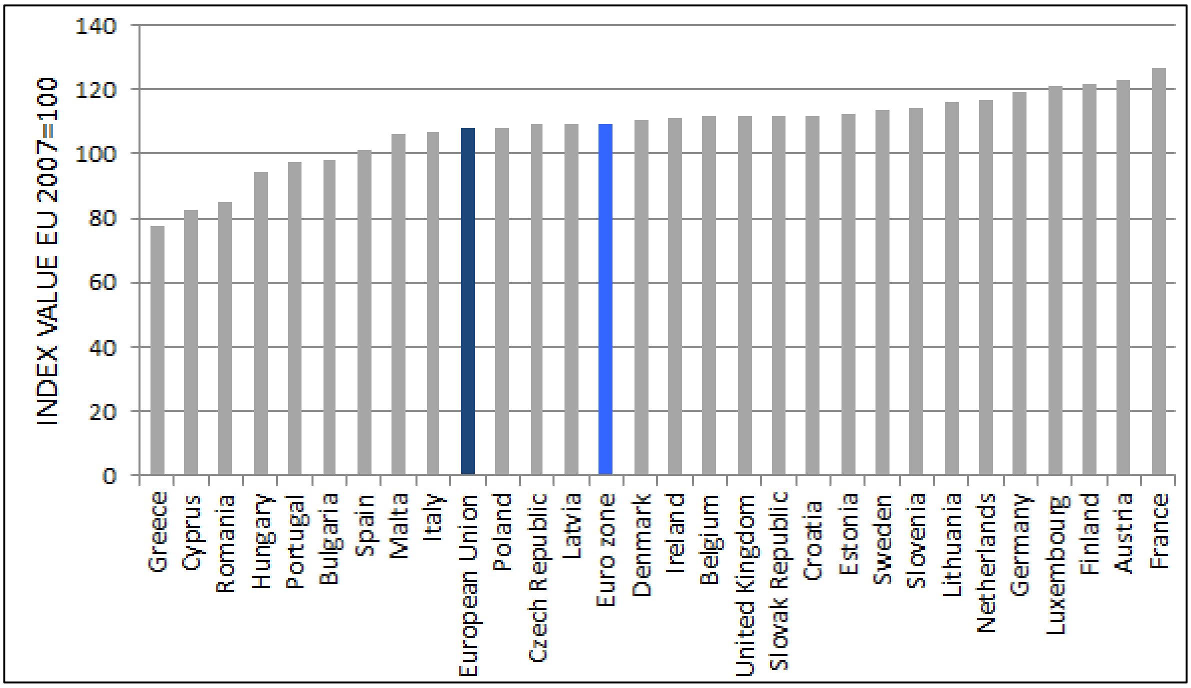
[12] European Commission (2015) A Framework Strategy for a Resilient Energy Union with a Forward-Looking Climate Change Policy, COM(2015)080 final

[13] This discussion is based on Kraemer-Eis H, Lang F, Torfs W and Gvetadze S (2016) European Small Business Finance Outlook June 2016, EIF Research and Market Analysis, Working Paper 2016/35 and the EC Survey on SMEs' access to finance (SAFE) 2014 edition.

of financing is relevant. Equity investment was the least preferred type of funding among SMEs with the ambition to grow. The ***cost of borrowing has continued to decline to record lows,*** but with significant country-level differences in the costs of finance. Although banks remain the key external financing source for SMEs, alternative financing instruments are gaining importance (including crowdfunding, debt funds, etc.). In almost all EU countries, SMEs face higher costs of finance than large firms.

Overall, according to the SMAF index developed by the EC, SMEs ***access to financial resources improved*** in 24 out of 28 Member States between 2007 and 2013.[14] The key driver seems to be the fall in interest rates for loans and overdrafts since 2009 for many EU countries. According to SMAF sub-indexes, debt finance has improved in 25 Member States outweighing the decline in the equity finance. Access to finance improved the most in France, Germany, and Lithuania and deteriorated in Greece, Romania and Hungary. Debt finance improved in all EU countries except Greece, Cyprus and Romania, while Spain has one of the least favourable equity finance environments.

Figure 2.6: SMAF index in 2013



Source: EC SMAF index

Supporting the provision of debt finance, ***guarantees*** continue to be widely, and increasingly, used, with the highest volumes in Italy and France. Italy and Portugal have the largest markets, related to GDP. New guarantee activity in 2015 was strongest (as a proportion of GDP) in Hungary, Portugal, Italy, Poland and Turkey.

Private equity investment has recovered over recent years, and in 2015, investments by private equity funds located in Europe increased by 13 percent to €47.4 billion, compared to 2014. Venture capital investments have increased by 11 percent to €4.0 billion. Business angel activity has grown to fill some of the gap left by venture capital investment after 2008. Exit markets have been strong in 2015; total divestments by

[14] The reference year of the SMAF Index is 2007 (EU 2007=100) allowing a comparison across countries, between Euro area and EU-28, and in time. 2007 was selected as a reference being the year before the start of the financial crisis. Thus, low values of the index indicate poor performance compared to the access to finance in EU level 2007.

private equity firms located in Europe increased, although there have been warnings of potential overheating. However, private equity and venture capital investment, and number of funds, remain well below the levels reached before the financial crisis. Related, government agencies accounted for 31 percent of total venture capital fundraising in 2015, supporting market recovery, but also highlighting the difficulty noted above in distinguishing public and private activity.

Beyond access to finance for enterprises, the private sector finances roughly two-thirds of ***infrastructure investment in the EU**,* in the form of debt (85 percent) and equity (15 percent). The debt funding market is dominated by banks. Bank lending for infrastructure projects has declined disproportionately since the crisis, due to deleveraging, new regulatory provisions and reduction of risk exposure – at the same time banks are reluctant to divest large amounts of existing infrastructure loan assets freeing up capacity for new lending. Further, some banks exited the market completely after the crisis.[15] The picture is similar for sustainable energy infrastructure, where the private sector accounts for roughly two-thirds of investment financing in OECD countries (debt or equity); this includes corporate sources such as electric utility companies and the financial sector (mostly banks). Investment here has also been constrained since the crisis and is expected to continue to diminish (from both public and private sources).[16]

2.2.2. National and EU sources of financial instruments

Within many EU Member States, the domestic public sector has long been involved in the provision of financial instruments (FIs) in the form of loans and guarantees (and more recently equity) in pursuit of economic development and other public policy goals. However, the scale of this finance is difficult to assess. The literature on the public sector provision of finance has tended to concentrate on grants, and there is a marked gap in the literature on the provision of alternative forms of finance including financial instruments.[17]

A wide range of different institutions is involved in the public sector supply of FIs, including national and regional development banks, public financial institutions, regional development agencies, guarantee providers, government departments, and standalone funds (see Annex 2). The boundaries between these institution types are blurred. There is considerable diversity in terms of length of experience,[18] some are small in scale and reach, while others are substantial and operate internationally.[19] Their geographical and sectoral remits also vary. Some, such as the *Land* banks in Germany, have an explicitly subnational remit. Others are nationwide in scope, but with a strong regional representation (Bpifrance, BGK in Poland). There is little standardised information

[15] Finance for Growth: Report of the High Level Expert group on SME and Infrastructure Financing, 2013.

[16] OECD (2015) Mapping Channels to Mobilise Institutional Investment in Sustainable Energy. Green Finance and Investment. OECD Publishing, Paris.

[17] Mazzucato M and Penna C (2015), The Rise of Mission-Oriented State Investment Banks: the cases of Germany’s KfW and Brazil’s BNDES, SPRU Working Paper Series SWPS 2015-26 (September), University of Sussex; Selyavina E (2014) What is a national development bank? Theoretical foundation and taxonomy design, ISJ Theoretical and Applied Science 12 (2) 47-52, ISPC European Research.

[18] Whittle M, Malan J and Bianchini D (CSES) (2016) *New Financial Instruments and the Role of National Promotional Banks*, Report to the European Parliament, Directorate-General for Internal Policies, Policy Department D, Budgetary Affairs.

[19] Michie R and Wishlade F (eds.) (2014) *Business Development Banks and Funds in Europe: Selected Examples: Briefing to the Scottish Government in the Context of the Scottish Business Bank Proposal*. European Policies Research Centre, University of Strathclyde.

available and systemic transparency is low,[20] making it difficult to compare the governance, remit and scale of the various entities. The environment within which public sector FIs are implemented is increasingly complex. Some funds and institutions operate transnationally and across borders, and are linked with other institutions through cooperation programmes, joint initiatives or provision of funding. Further, EU funding sources also use domestic institutions and financial intermediaries within Member States and regions to deliver finance to final recipients.[21]

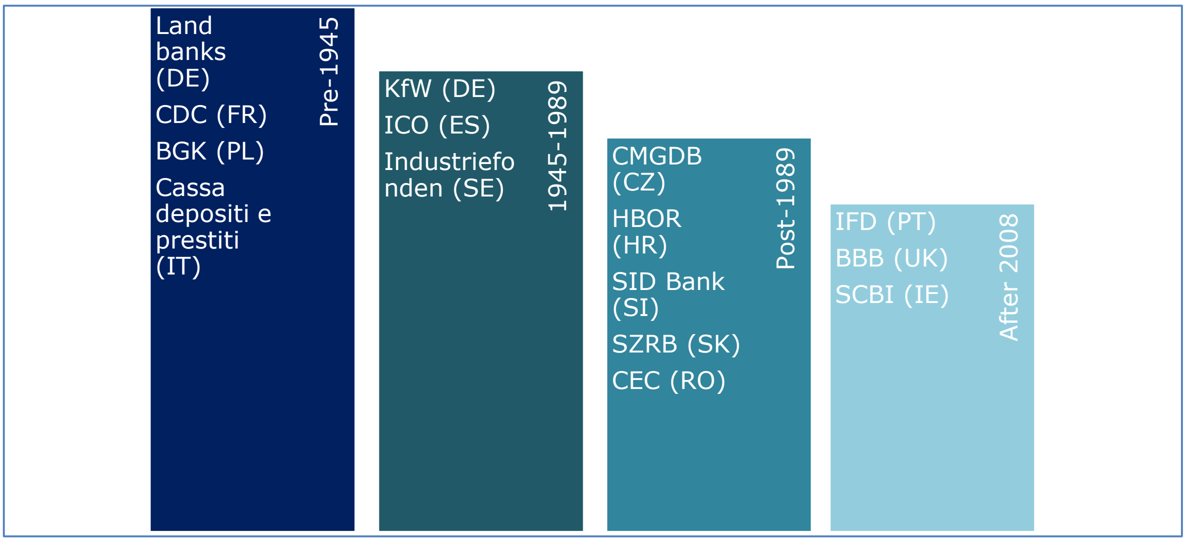
2.2.3. What institutions are involved in the supply of public FIs?

The institutions delivering public sector FIs vary widely in structure and function,[22] making comparisons difficult, but three broad groupings can be identified:

- ***Public financial institutions***, which operate more than one fund (or funds of funds) and often collaborate with other organisations, but whose focus remains on business development, especially SMEs. Examples include Finnvera (FI), Land business banks (DE), Bpifrance (FR), the Strategic Banking Corporation of Ireland (IE), and Finance Wales and the British Business Bank (UK).
- ***Investment funds*** with a remit essentially limited to SME development – for example, Innovation SME+ (NL), *Vaekstfonden* (DK) and *Industrifonden* (SE).
- ***Public banks***, whose operations are on a more significant scale and extend into areas beyond SME development into infrastructure, lending to local authorities and potentially international operations, examples include KfW (DE), BGK (PL), ICO (ES), and *Land* banks (DE).

In reality, the boundaries between these groups is blurred, and whether institutions providing public sector FIs operate as 'agencies' or are set up as 'funds', they remain a 'concept rather than a fixed category', and can be most usefully distinguished by their mission of promoting economic development and other socio-economic goals.[23]

Figure 2.7: Development of institutions supplying public-sector FIs



[20] Wruuck P (2015) *Promoting Investment and Growth: The role of development banks in Europe*, EU Monitor Global Financial Markets, Deutsche Bank Research.

[21] Ibid.

[22] Schmit M, Gheeraert L, Denuit T, Warny C (2011) *Public Financial Institutions in Europe*, European Association of Public Banks, Brussels.

[23] Ibid.

The public sector has long been involved in the supply of FIs in many developed economies, and national promotional banks have 'traditionally been part of the economic policy toolkit and the financial market landscape'.[24] Some of the oldest institutions are of very longstanding. For example, the German *Land* banks were created in the late 19th century and the French *Caisse des dépôts et consignations* (CDC), which owns 50 percent of the present day Bpifrance, can be traced back to 1816. The Italian *Cassa depositi e prestiti* was founded in 1850, and the Polish *Bank Gospodarstwa Krajowego* (BGK) in 1924.

Box 2.1: The State Development Bank of Poland (BGK)

The decree establishing BGK was issued in 1924, when it was created by a merger of three existing public banks the Polish National Bank, the State Reconstruction Bank, and the Credit Institution of Malopolska Cities. BGK's operation was suspended from 1948 as a result of banking reform, but in 1989, BGK resumed operation as a State-owned bank, acting as the issue agent for Treasury bonds. BGK's mission is to support the social and economic growth of Poland and to provide services to the public finance sector. As such, BGK actively participates in the implementation of the state's economic objectives, and manages several special purpose funds and a number of governmental programmes.

Several large institutions and funds were set up in EU Member States during the post-war period, including KfW (Germany), ICO (Spain), and *Industriefonden* in Sweden. This was followed by a further wave of wave of institutions set up in Central and Eastern European countries after 1989, to promote the transformation of transition economies (for example, in the Czech Republic, Croatia, Slovenia, Slovakia and Romania).

Box 2.2: The Czech-Moravian Guarantee and Development Bank

The Czech-Moravian Guarantee and Development Bank was established in 1992. Its goal is to provide financial assistance to SMEs, development of infrastructure and other economic sectors in accordance with the economic policy of the Government of the Czech Republic. The Bank is 100 percent State-owned and operates at national level. The Czech-Moravian Guarantee and Development Bank's long-term goals and primary business are focused on providing assistance to SMEs with the aim of enabling easier access to financial capital, sharing business risk and reducing project costs through support tools such as bank guarantees, preferential loans and financial subsidies. The Bank also participates in the implementation of State policy aimed at financing specific projects helping to improve regional technical infrastructure and reconstruction of panel-block apartment buildings.

New impetus to the growth of national promotional banks was given by the economic crisis, when many public sector institutions provided counter-cyclical funds as commercial banks curtailed their lending. A new 'foundational phase' has since been launched, with some Member States setting up new institutions (e.g. Ireland, Portugal and the UK), others reorganising existing institutions (e.g. France, Latvia), and a number of countries considering changes and/or setting up new development/ promotional banks (e.g. Malta, Greece). [25]

Box 2.3: Strategic Banking Corporation of Ireland

The Strategic Banking Corporation of Ireland (SBCI) was formally launched in 2014, in the wake of Ireland's exit from the EU/IMF financial support programme. It is a new, strategic SME funding company, aiming to ensure access to flexible funding for Irish SMEs. Its objective is to support sustained SME-led economic performance in Ireland following the recession. Initial funding partners include the EIB (€400 million), KfW (€150 million) and the Ireland Strategic Investment Fund (ISIF) (€350 million). ISIF has also provided €10 million in equity capital to fund SBCI start-up costs. SBCI will source funds externally through its three funders and lend them to SMEs through

[24] Wruuck P (2015) Op cit.

[25] Ibid.

loans via other institutions (on-lenders). On-lenders may be retail banks or other organisations which have the ability to assess loan proposals from SMEs.

Public involvement ranges from minor participation to full control. When analysing the scope of public financial institutions in the (then) EU27 plus Croatia, Macedonia, Norway, Switzerland and Turkey, Schmit *et al* took account of the actual level of control rather than just level of ownership, and the 'continuous spectrum of public influence'.[26] The analysis estimated that the assets of the *publicly influenced* financial sector amounted to €9,883 billion (21 percent of total bank assets), with over half of this pertaining to public institutions. Full public ownership is the prevalent model among the European promotional banks and is largely a reflection of their founding history and evolution rather than regional patterns.[27] In some countries, public sector involvement is through many institutions (DE, ES, IT) while in others, the role is concentrated in fewer bodies (e.g. Kredex in Estonia, INVEGA in Lithuania).[28]

Models vary widely between Member States. For example, in Germany and Spain there are networks made up of relatively high numbers of regional institutions which are well embedded in local banking activities; by in contrast, in the UK, Ireland and the Nordic countries there is relatively little government intervention. In Central and Eastern European countries, the public sector has a strong influence over a few institutions with a specific focus.[29]

Detailed governance arrangements vary between organisations, notably the extent of government involvement and the relationship with relevant ministries; it is worth noting that this relationship can change over time as institutions become more embedded (e.g. the British Business Bank was initially set up in as a 'programme' run directly by the UK's Department for Business, Innovation and Skills; once State aid clearance was granted, the programme was transferred to the British Business Bank, which now operates as a Government-owned financial institution). Institutions can also move out of the public sector, as with the Green Investment Bank in the UK (see below). Some institutions/funds remain directly run by a national ministry (e.g. *Vaekstfonden*, Finnvera, *Industriefonden*) while others operate as independent legal entities with State-appointed board members (the German *Land* banks and *Land* business development banks).[30]

Box 2.4: Green Investment Bank, UK

The Bank was launched in November 2012. With capital from the UK government, it was the first bank of its kind in the world - a "for profit" bank, whose mission is to accelerate the UK's transition to a greener economy, and to create an enduring institution, operating independently of government. UK Government provided the Green Investment Bank with initial capital to invest in green projects, on commercial terms, across the UK and stimulate mobilisation of other private sector capital into the UK's green economy. The Bank is seen as a key part of the UK's efforts to achieve its environmental targets. The UK Government committed an initial £3.8 billion in the Bank. By 2014, the Bank had invested in 26 projects, directly investing £1.3 billion. Target sectors included: offshore wind; energy efficiency; waste and bioenergy; and onshore renewables. In March 2016, the UK Government launched the process to move the Green Investment Bank into the private sector. The transaction will involve both the sale of existing shares owned by the UK Government and also the commitment of additional capital for the Green Investment Bank by new investors.

[26] Schmit et al (2011) Op cit.

[27] Wruuck P (2015) Op cit.

[28] Schmit et al (2011) Op cit.

[29] Ibid.

[30] Michie R and Wishlade F (eds.) (2014) Op cit.

Most institutions operate indirectly through private actors or combine both indirect and restricted direct funding.[31] Indirect models are most popular where relationship banking is strong and where there is a network of commercial institutions to work with. This is the case in Germany, for example, with *Land* banks having strong links into the local commercial banking sector.

2.2.4. What type of project/investment can public FIs support?

The ***remit of the public sector organisations involved is expanding***. The original rationale and remit of some of the older institutions involved in the provision of public sector FIs was often rooted in major historical crises – for instance, the need to safeguard public funds following the collapse of the Napoleonic empire lay behind the CDC in France, or support for post-war reconstruction in the case of the KfW in Germany.[32] Currently, public sector financial institutions acting in domestic markets set out to fulfil a wide variety of missions, including addressing finance gaps, supporting the agricultural sector, developing infrastructure, promoting tourism, and supporting financial inclusion in regional markets.[33] This role has diversified in the past three decades, going beyond traditional activities in both scale and scope,[34] extending to playing an important part in addressing current societal challenges, especially around innovation, energy and the green economy.[35]

SME lending remains the predominant activity of most of the institutions concerned, especially when 'commercial banks have partially or fully withdrawn from the SME lending space.'[36] Newer institutions tend be more focused on business development (i.e. infrastructure or local authority lending is not part of their remit), and some have been born directly out of concerns with issues of access to finance – for example, SBCI (IE), which was a direct response to the financial crisis in Ireland. Public institutions have also increasingly become involved in providing long-term venture capital for high-tech start-ups (the so-called 'gazelles'), and are lead funders of 'mission-oriented innovation' in some countries in the push towards smart growth.[37]

Guarantees are the most widely used instrument by public sector institutions.[38] Governments have used credit guarantee schemes since the 1950s, usually targeting a sector, region, or type of firm. Public guarantee schemes have also been the most widely used instrument of government policy to ease SME access to finance in the crisis.[39] In some cases this involved easing the terms – for instance, in France, Oséo (now Bpifrance) increased the maximum guarantee cover to 90 percent, while in Italy eligibility criteria were relaxed and in many countries loans to finance working capital needs were guaranteed.[40]

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[31] Ibid.

[32] Ibid.

[33] Schmit et al (2011) Op cit.; Selyavina E (2014) Op cit.

[34] Mazzucato M and Penna C (2015) Op cit.

[35] Selyavina E (2014) Op cit.

[36] Whittle M, Malan J and Bianchini D (CSES) (2016) Op cit.

[37] Mazzucato M and Penna C (2015) Op cit.

[38] Trentinaglia M T (2015) 'Institutions' in Navaretti G (Ed) (2015) Who takes the risks for funding SMEs?, *European Economy, Regulation and the Real Sector 2105.2*.

[39] Kraemer-Eis, H, Lang, F and Gvetadze, S (2014) 'European Small Business Finance Outlook', *EIF Working paper 2014/26*.

[40] OECD (2013) *SME and Entrepreneurship Financing: The Role of Credit Guarantee Schemes and Mutual Guarantee Societies in supporting finance for small and medium-sized enterprises*.

The most widely used data available on guarantees is that produced by the European Association of Mutual Guarantee Societies (AECM). This covers the activities of its members which are predominantly publicly-owned bodies. Guarantees appear to be most significant in Hungary, Portugal and Italy, with outstanding guarantees in the order of 1.5 to 2 percent of GDP. In Italy, public guarantees on SME loans rose from around €2 billion in 2007 to €12 billion by 2014.[41] Finland, Germany and the Netherlands also relied heavily on public guarantee schemes to compensate for the reduction in private bank lending during the economic crisis.[42] Use of counter-guarantee schemes is much less common,[43] but prevalent in Italy and also used in Belgium.

Loans are also widely used, but provision of venture capital and equity FIs more generally is far less common – Belgium, Sweden and the UK have until recently been the main actors in this respect.

2.2.5. What is the scale of public FIs?

The ***relevant institutions vary widely in terms of scale and importance***. There is no transparent and easily comparable treatment of promotional banks in national statistics, which limits the possibility for comparison across countries, and makes it difficult to assess their role and significance.[44] Comparison of scale and budgets of such institutions can be misleading, in particular because it does not reflect the importance of a particular institution/fund to the economy in which it operates – small institutions can play an important role, or have a large share of a specific market.[45] However, in terms of scale, among the most prominent bodies are several of the German *Land* Banks (up to €274 billion of assets by the end of 2013) and the *Land* business development banks (up to €145 billion) (see Figure 2.8).

[41] Navaretti G, Calzolari, and Pozzolo A (2015) Is special treatment of SMEs warranted? in Navaretti G (Ed) (2015) Who takes the risks for funding SMEs?, *European Economy, Regulation and the Real Sector 2105.2*.

[42] OECD quoted in Gozzi J and S Schmuckler (2015) Public Credit Guarantees and Access to Finance in Navaretti G (Ed) (2015) *Who takes the risks for funding SMEs?, European Economy, Regulation and the Real Sector 2105.2*.

[43] Gozzi J and S Schmuckler (2015) ‚Public Credit Guarantees and Access to Finance in Navaretti G (Ed) (2015) *Who takes the risks for funding SMEs?, European Economy, Regulation and the Real Sector 2105.2*.

[44] Wruuck P (2015) Op cit.

[45] Ibid.

Figure 2.8: Scale of public FIs (selected examples)

Member State	Institutions	Capitalization (€ billion)	Population (million)	GDP (€ billion)
DE	*Land* Banks *Land* Business Development Banks KfW	from 17 to 274 (2013) from 1 to 145 72.5 (2013)	82.0	2,737
DK	*Vaekstfonden*	0.36	5.6	249
ES	ICO	from 53 (2008) to 102 (2013)	46.7	1,023
FR	BPI France Bpi Financement Bpi Participations	51.5 (end of 2013) 34.7 16.8	65.6	2,060
IE	SBCI	0.8 (October 2014)	4.6	164
PL	BGK	2 (2014)	38.5	390
SE	*Industrifonden*	0.408	9.6	421
UK	British Business Bank	5 (to 2018+)	63.9	1,899

Note: IE: set to increase by €5 billion over the next five years. GDP figures 2013. **Source:** Eurostat and Quarterly National Accounts and based on Michie R and Wishlade F (eds.) (2014) Op cit.

In terms of ***sources of funding***, national and regional promotional banks are not necessarily limited to public funds, but may also be able to access (inter)national financial markets – facilitated in many cases by State guarantees, allowing them to borrow at favourable rates.

Box 2.5: How Finnvera is funded

Finnvera was set up in 1999 through the merger of Kera Corporation (*Kera Oyj*) and the Finnish Guarantee Board (*Suomen Valtiontakuukeskus*). Kera Corporation provided loans and guarantees for domestic business activities while the Finnish Guarantee Board was responsible for export credit services. The merger took place in order to reorganise the administration of publicly supported special financing, to improve the efficiency and effectiveness of the State's special financing and to streamline the State's corporate governance. Finnvera is expected to be economically self-sufficient (i.e. in the long run, it must be able to cover its own operating costs and credit and guarantee losses with the income from commercial activities). The State currently covers c.50 percent of Finnvera's domestic credit losses. Other losses and operational costs are to be covered by profits. Finnvera borrows on domestic financial markets to fund its activities. However, the State is directly responsible for the domestic guarantees and export credit guarantees granted by Finnvera.

In addition, increasing 'Europeanisation' is evident, as many national and regional financial institutions that deliver FIs using domestic funds co-fund them with ESI Funds or manage EU FIs (see Figure 2.9), or are involved in implementation of the joint SME Initiative with the EIB.

Figure 2.9: Examples of institutions using ESIF in 2007-13/2014-20

MS	Institutions involved
BE	SOWALFIN (Société Wallonne de Financement et de Garanties des PME), created in 2002 to support SMEs via specific FIs was Intermediate Body for Wallonia ERDF OP and delegates management of FIs to subsidiaries, the 'Invests' – investment funds part-owned by SOWALFIN managed FIs under ERDF 2007-13 OP, as did SOCAMUT and NOVALIA, subsidiaries of SOWALFIN and providers of micro-credit, loans and guarantees.
CZ	Czech-Moravian Guarantee and Development Bank implemented ERDF FIs in 2007-13.
DE	*Land* Banks and *Land* business development banks use ESI funds to co-finance some FIs.
EE	Kredex, a national fund acting as NPB, implemented ESIF FIs in 2007-13.
ES	ICO, a national state financial agency and intermediated lender, managed an EU-funded JEREMIE fund in 2007-13, offering guarantees on RTDI projects.
FI	Finnvera used EU funding to offer interest subsidies on loans in 2007-13, as well as co-investments in venture capital instruments.
HU	Hungarian Development Bank is Fund of Funds manager for ESIF FIs in 2014-20
IT	Invitalia, national promotional agency, was responsible for management of national directly-managed FIs in 2007-13 (e.g. NOP R&C funds 2007-13). Medio Credito Centrale (Banca del Mezzogiorno MedioCredito Centrale S.p.A. (BdM-MCC)) has also been involved with ESIF FIs through the co-funded Fondo Centrale di Garanzia (FCG).
LT	INVEGA managed the Entrepreneurship Promotion Fund, which used ESIF.
PL	BGK (Bank Gospodarstwa Krajowego) has been holding fund manager for JESSICA and JEREMIE initiatives, and has served as a paying authority for Structural Funds.
PT	The Institução Financeira de Desenvolvimento (IFD) was set up to manage ESIF FIs in 2007-13. PME Investimentos – Sociedade de Investimento, S.A, a credit institution under the supervision of the Bank of Portugal, was FINOVA Holding Fund manager in 2007-13.
SE	Almi Invest a key provider of State equity capital in Sweden was fund manager of the regional risk capital funds co-financed by ESIF in 2017-13.
SK	The Slovak Guarantee and Development Bank implemented FIs in 2007-13 and 2014-20.
UK	British Business Bank managed some ERDF legacy funds from 2000-06 and 2007-13, and will manage several ERDF-funded FoF in 2014-20. Scottish Investment Bank (Scottish Enterprise) managed ERDF-funded FIs in 2007-13, and may also fund manage in 2014-20. Finance Wales managed the 2007-13 EU-funded JEREMIE Fund in Wales and has been entrusted with management of the Wales SME Investment Fund in 2014-20. INVEST NI, a regional development agency and Intermediate Body for ERDF uses ESIF to co-fund three of their six Access to Finance funds for SMEs.

Source: EPRC compilation

2.2.6. What is the role of EU-level institutions?

The environment has become more complex with ***a larger role being played by the EU institutions**,* which are increasingly involved in the supply of FIs. This is both under in their own name and through intermediaries, increasingly national promotional banks. The European Investment Bank Group (EIB Group) plays an important role, and is central to the implementation of most EU-level FIs (while the Commission maintains overarching responsibility).[46] The EIB currently has a dual role: as an investment bank which can offer loans at low cost to its borrowers due to its AAA status; and as a public institution tasked with implementing broader European policy objectives such as economic development, climate-change prevention, employment generation, financing SMEs and convergence.[47] The role of the EIB in Cohesion policy has progressively expanded since the early 2000s, and now includes provision of long-term loans to public and private project promoters, framework loans to public authorities, intermediated loans providing

[46] Whittle M, Malan J and Bianchini D (CSES) (2016) Op cit.

[47] van der Zwet A, Bachtler J, Miller S, Vernon P and Dozhdeva V (2016) *The role of European Investment Bank Group in European Cohesion Policy*, report to the European Parliament, REGI Committee.

credit lines to banks and leasing bodies to on-lend, and global loans managed by intermediaries, usually financial institutions.[48]

Alongside the EIB, the European Investment Fund (EIF) is a public-private partnership owned by the EIB (61.3 percent), the EU through the European Commission (26.5 percent) and 29 public and private institutions (12.2 percent). The last category includes financial institutions such as Barclays Bank plc in the UK and Banco Santander in Spain, as well as national/regional promotional banks (e.g. BGK in Poland, Bpifrance and some of the German *Land* banks) as well as development agencies (e.g. Scottish Enterprise in the UK).[49] Supporting SMEs and midcap finance is the EIB Group's single largest policy priority in terms of activity volume.[50] In 2014, the EIB Group's support to SMEs amounted to €28.1 billion (new operations signed) of which €3.3 billion from the EIF, supporting over 290,000 SMEs.

The EIB and EIF are also involved in managing EU-supported FIs as 'entrusted entities'; the EIB focuses on the provision of loan and debt-based instruments to mid-caps while the EIF deals with loan guarantee schemes (such as COSME, InnovFin, Creative Europe, EaSI, Erasmus+ and PF4EE) as well as equity instruments such as the COSME Equity Facility for Growth, and implements its own venture capital fund of funds programme (Figure 2.10).[51] These FIs are generally implemented through financial intermediaries, including national/regional development banks, and ultimately commercial banks, who on-lend to SMEs and project promoters. Institutions using these funds may 're-brand' them, reducing transparency about the source of funds.

Box 2.6: National implementation of InnovFin SME Guarantee Scheme in France

BPI has signed two agreements with the EIF in relation to the InnovFin SME Guarantee scheme. Under the agreement they will provide finance to innovative companies in France worth €420 million between 2015-17, guaranteed by the EIF. Bpifrance has branded the two loan FIs at national level as part of its own product portfolio, which is then marketed directly to SMEs. These comprise: ***Start-up loan*** (*Prêt d'Amorçage investissement*) to address financing needs of start-up companies. Bpifrance will combine this FI with the EU guarantee at a 40 percent rate. ***Innovation loan*** (*Prêt pour l'innovation*), an existing loan programme which will be increased in scale in terms of beneficiaries and loan maxima, backed by the EU guarantee at a 50 percent rate.

Source: Whittle M, Malan J and Bianchini (2016) Op cit.

The picture has become more complex with the launch in July 2015 of the ***European Fund for Strategic Investments (EFSI)*** as part of the Investment Plan for Europe. The Commission has made €16 billion available, and the EIB has provided an additional €5 billion for EFSI, which provides a guarantee for the EIB to extend its 'special activities' portfolio. The funds that provide the guarantees are derived from re-allocated resources (the Connecting Europe Facility and Horizon 2020). The funds are used to allow the EIB to invest in higher-risk projects (special activities). However, EFSI itself is not a financial instrument (within the meaning of the EU Financial Regulation), although it can be invested in FIs.[52]

[48] van der Zwet A, Bachtler J, Miller S, Vernon P and Dozhdeva V (2016) Op cit.

[49] van der Zwet A, Bachtler J, Miller S, Vernon P and Dozhdeva V (2016) Op cit.

[50] Revoltella D and H Kraemer-Eis (2015) Tackling SMEs asymmetric risk: the EIB approach, in Navaretti G (Ed) (2015) *Who takes the risks for funding SMEs?, European Economy, Regulation and the Real Sector 2105.2*

[51] Entrusted entity status for the indirect management of EU FIs is apparently being considered by the Commission for other entities such as EBRD (Whittle M, Malan J and Bianchini D (CSES) (2016) Op cit p10).

[52] Ibid.

The EIB and EIF both play an important role in delivering EFSI; national development/promotional banks can also be involved by co-investing alongside the EFSI in strategic investment projects of interest in their respective Member State.[53] Member States can contribute to EFSI, either directly or via their national development/promotional banks. They can contribute either at the level of projects, FIs or investment platforms.[54] By June 2016, eight Member States had pledged contributions to EFSI via their national promotional banks: Bulgaria €100 million, Slovakia €400 million, Poland €8 billion, Luxembourg €80 million, France €8 billion, Italy €8 billion, Spain €1.5 billion, Germany €8 billion, plus the UK announced it would make a guarantee available to co-finance infrastructure projects in the UK (not via promotional bank).[55] According to the Commission, national promotional banks have expressed a clear preference for cooperating at the level of investment platforms and on the level of individual projects rather than direct participation.[56]

It is clear that while the EIB and EIF are responsible for injecting large volumes of funding into the supply of FIs in EU Member States, the bulk of the FIs are delivered through national or regional institutions.

In summary, there are a wide variety of sources of funds (EU, domestic) being delivered through a complex web of institutions and intermediaries, including commercial banks and private sector fund managers. The number, range and remits of these organisations, coupled with a lack of transparency in the ultimate source of funding – partly owing to domestic practices of 'rebranding' funds - makes it very difficult accurately to assess the scale of funds available, and the additionality of any new funding stream that is announced. Most of the EU institutions and national promotional banks discussed above do not lend directly, rather on-lend through commercial banks and financial intermediaries. The effect of public sector intervention should be to increase the supply available at the level of the SME or project promoter. This complexity may be irrelevant to the SME or project promoter who may be unaware of the source of funds. However, from a policy analysis perspective, it renders the task of differentiating between *public* and *private* sector sources of funding and quantifying the overall scale of available funds quite impossible.

[53] Potential investment projects are presented to EIB or EIF by project promoters. EIB/EIF internal governing bodies and the EFSI Investment Committee decide on granting of EFSI support.

[54] Investment platforms are special-purpose vehicles, managed accounts, contract-based co-financing or risk-sharing arrangements or arrangements established by any other means by which entities channel a financial contribution in order to finance a number of investment projects (Art. 2, 2015/1017).

[55] European Commission (2015) *Working together for jobs and growth: The role of National Promotional Banks (NPBs) in supporting the Investment Plan for Europe*.

[56] Ibid.

Figure 2.10: EU-level FIs in 2014-20 and the role of NPBs

EU-level FI	Implementation details	Scale
COSME Loan Guarantee facility	Guarantees and counter guarantees provided to financial intermediaries, who on-lend loans and leases to high-risk SMEs. So far, several national promotional banks are involved: AWS (AT), CMZRB (CZ), Danish Growth Fund, Kredex (EE), KfW and Bürgschaftsbank Nordrhein-Westfalen (DE), SCBI (IE), Cassa depositi e prestiti (IT), BGK (PL). Strong participation by commercial banks.	Over €19.3 billion in loans and over 340,000 SMEs supported since 2007 under predecessor scheme (SME Guarantee Facility).
COSME Equity Facility for Growth	Invests in venture capital and private equity funds, which act as financial intermediaries to provide funding to SMEs, predominantly in their expansion and growth stages. No information yet on participation.	Over €2.3 billion in equity investments mobilised since 2007 under predecessor scheme (High Growth and Innovative SME Facility).
InnovFin SME Guarantee Facility (Horizon 2020)	Provides guarantees and counter-guarantees to financial intermediaries, who provide loans, financial leases and loan guarantees for research-based and innovative SMEs and small mid-caps. So far, numerous national promotional banks have signed agreements with the EIB to act as intermediaries. E.g. AWS (AT), Danish Growth Fund, Bpifrance, KfW and Bürgschaftsbank Baden-Württemberg (DE), SCBI (IE), Cassa depositi e prestiti (IT, BGK (PL), British Business Bank (UK).	The predecessor scheme (RSFF) financed 114 R&I projects with €11.3 billion and provided loan guarantees worth over €1.4 billion.
Natural Capital Financing Facility (LIFE)	Loans and investments funds that support projects promoting the preservation of natural capital. No interest as yet from national promotional banks or commercial banks – may be targeted at specialist financial advisers and micro-credit institutions instead.	Small pilot scheme; will only support 10 projects across EU28.
Private Finance for Energy Efficiency Instruments – P4EE (LIFE)	Loan guarantee facility for energy efficiency investments. Only commercial banks can take part.	Not available to national promotional banks.
Cultural and Creative Sector Guarantee Facility (CCS LGF)/Creative Europe	Aims to encourage greater lending to SMEs in creative and cultural sectors via credit risk protection through a capped guarantee and capacity building. National promotional banks can apply to become financial intermediaries.	

Sources: Whittle M, Malan J and Bianchini D (CSES) (2016) Op cit; van der Zwet A, Bachtler J, Miller S, Vernon P and Dozhdeva V (2016) *Op cit.*

Figure 2.11: Selected EIF Fund of Funds

MS	Title	Operation
EE, LT, LV	Baltic Innovation Fund	Launched by the EIF with the Governments of Lithuania, Latvia and Estonia in 2012 to boost equity investments made into Baltic SMEs with high growth potential. BIF represents a €52 million investment by EIF with each Baltic Government committing €26 million through national agencies (INVEGA in Lithuania, KredEx in Estonia and Altum in Latvia). A significant part of the resources committed by national agencies are returned resources from earlier Structural Funds financed financial instruments under JEREMIE framework, now being reused.
NL	Dutch Venture Initiative (DVI-II)	A €200m venture and growth capital Fund of Funds initiative of the EIF and PPM Oost, supported by the Dutch Ministry of Economic Affairs. Launched in March 2016, it aims at investing in fast growing and/or innovative companies, targeting companies in sectors such as ICT, clean-tech, med-tech, renewable energy and life sciences, through primary investments in Dutch-oriented VC funds.
LU	Luxembourg Futures Fund (LFF)	A €150m fund set up by the EIF and the SNCI which will invest and co-invest in early and growth innovative European technology SMEs as well as in VC funds. LFF invests directly or indirectly in VC funds and SMEs to foster the sustainable development of strategic sectors (i.e. ICT, cleantech and other technology sectors excluding health technologies and life science sectors).
PL	Polish Growth Fund of Funds	A €90m Fund of Funds initiative launched in April 2013 by the EIF with BGK to stimulate equity investments into growth-focused enterprises in Poland. Locally, the initiative is named *Polski Fundusz-funduszy Wzrostu* (PFFW). At the initial stage, PGFF combines a €30 million commitment from EIF with €60 million from BGK.
SE	Swedish Venture Initiative	The Swedish Venture Initiative combines ESIF resources with EFSI. The Swedish Venture Initiative will invest using ESIF in several early stage venture capital funds which will then invest primarily in Swedish enterprises. Co-investment from EFSI by the EIF into the underlying funds will encourage private investors to commit additional resources into these funds. It is expected that more than SEK 1 billion in equity investments will be made available to the Swedish enterprises.

Source: EIF

2.3. What is the economic rationale for using financial instruments in Cohesion policy?

In addressing this question, it is useful to consider three interrelated 'sub-questions' in order to tease out the key issues, more specifically:

- What is the justification for public intervention at all?
- If intervention is justified, to what extent can the aims of intervention be met, or met better, by financial instruments as opposed to non-repayable funding?
- What are the rationales for co-financing FIs under Cohesion policy?

2.3.1. What is the justification for public intervention?

In broad terms the justification for public intervention in economic development policy is to support activities that market operators cannot or will not undertake alone, but which are considered in the wider public interest. This is sometimes characterised as 'market failure', but in fact can arise in situations where there simply is no market and the private sector is operating quite rationally, or where the market is imperfect and operating sub-optimally. These include the following:[57]

The provision of ***public goods.*** These are generally defined as 'non-excludable' and 'non-rivalrous', meaning that access to the goods concerned cannot be limited to those who pay for them and their use by one party does not diminish their availability to others. Classic examples of public goods include lighthouses and street lighting, but clean air, and certain types of public infrastructure such as flood defences might also be considered public goods since there is no scope to create an efficient market for them.

The supply of ***merit goods,*** that is, those goods and services which governments consider would be consumed at a lower level than desirable if determined solely by the free market, and where public authorities should intervene in order to ensure uptake at optimal levels. Examples include aspects of education, culture, health services, museums and libraries.

The presence of ***externalities*** - the notion that the activities of an individual or an undertaking have spillovers which affect others and that these are not reflected in market prices. In other words, commercial assessments of returns on investment do not necessarily capture the wider social or longer term benefits. The conventional example of a positive externality is research and development. Firms may be deterred from investing in R&D because they cannot reap all the gains from their investment (assuming a successful outcome) and there are risks that others will 'free ride' on their innovation. This may result in suboptimal levels of investment in R&D, and yet the dissemination of new technology has wider societal benefits justifying public sector intervention to provide, among other things, the 'patient long-term finance' important for innovation.[58] Similarly, firms may be discouraged from bearing the costs of vocational training to the extent that it increases the likelihood of staff being 'poached' by other employers who have made no such investment, and yet there are wider benefits to society (and individuals) of a better skilled workforce. Further examples are urban development or energy efficiency projects which offer longer-term societal and environmental gains that justify public intervention, but might not attract sufficient commercial funding.

Imperfect information in financial markets. Of course, 'perfect' information is a purely theoretical construct, and risk aversion where insufficient information is available is a rational market response by an investor. However, information asymmetries can be particularly acute among start-ups who have no track record and new firms in high technology sectors, where the risks are difficult to assess precisely because their activities are innovative. Such firms often lack the collateral needed to secure capital or the cost of capital is too high because of their risk profile; analysis has suggested that access to finance is likely to be especially difficult for certain categories of SME, notably start-ups, small and/or young firms, high tech enterprises.[59] This is an important policy consideration because there has been increasing policy focus, at European, national and subnational levels on the nurturing of high growth firms.[60] This reflects the fact that a very small proportion of new firm starts will account for the majority of benefits in terms

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[57] Meiklejohn, R. (1999) *The Economics of State Aid,* in 'State aid and the Single Market', European Economy, 3.

[58] Mazzucato M and Penna C (2015), The Rise of Mission-Oriented State Investment Banks: the cases of Germany's KfW and Brazil's BNDES, *SPRU Working Paper Series SWPS 2015-26* (September), University of Sussex.

[59] Siedschlag, I et al (2014) *Access to External Financing and Firm Growth*, background study for the European Competitiveness Report 2014, ESRI.

[60] OECD (2010) *High Growth Enterprises: What governments can do to make a difference*, Paris: OECD.

of investment, employment and exports,[61] but significant numbers of ambitious new firms cite access to finance as a constraint on their development.[62] This focus also partly reflects the role that private venture capital is considered to have played in the development of high technology firms in certain locations - like Silicon Valley and Israel - and in the development of some high profile firms such as Google and Facebook.[63] Indeed, concern has long been expressed at the relative underdevelopment of venture capital markets in European countries,[64] and at the role of space and place in the availability of capital, with capital heavily concentrated in the more prosperous areas.

In practice, two or more of these situations justifying public intervention may be present simultaneously. For example, information asymmetries may mean that assessment of very small projects requiring microfinance incur disproportionate transaction costs for investors, leading to a dearth of funds for initiatives that could have a positive impact on society by reintegrating individuals into the labour market supporting disadvantaged groups and/or reducing welfare dependency.

2.3.2. Can the aims of intervention be met better by financial instruments than grants?

The second 'sub-question' concerns the ***form of intervention***. From a *policy design* perspective, repayable funds are *an alternative delivery mechanism* to grants. It is important to highlight this, since the use of financial instruments is often cast in terms of addressing a 'gap' in access to finance – typically difficulties that SMEs have in accessing loan funding or investment capital. However, grants can also be used to address gaps in access to finance and the key issue here lies not in the *objective* of funding per se, but rather in what difference the delivery mechanism can make to the achievement of that objective and wider policy effects.

Box 2.7: What are the rationales for choosing grants or financial instruments?

Grants and financial instruments play different roles in economic development, but their purposes also overlap.

Grants can be used to address a range of market imperfections – the undersupply of public goods or merit goods, as well as externalities such as training or research and development or information asymmetries resulting in insufficient access to capital.

Financial instruments are only viable where the purpose to which they are put has the potential to generate revenue or savings which can be used to repay the original outlay – for example, successful commercialisation of an innovation or cost savings from energy efficiency investments. The revenue-generating requirement tends to limit the use of financial instruments to certain types of market imperfection – notably those related to externalities or information asymmetries.

In these areas financial instruments can, at least partially, replace grants as a policy delivery mechanism. This has several advantages. In particular:

- From a budgetary point of view financial instruments should be more sustainable than grants
- The need to repay support may lead to better quality projects
- Financial instruments can be used to cover the totality of investment needs for economic activities, while for grants the scope of funding will be limited by the State aid rules

[61] Henrekson, M and Johansson, D (2010) *Gazelles as job creators: a survey and interpretation of the evidence*, Small Business Economics, 35 (2), 227-244.

[62] Maula, M, Murray G and Jääskeläinen M, (2007) *Public financing of young innovative companies in Finland*, Ministry of Trade and Industry, Helsinki, Publication 3/2007.

[63] Gompers, P and Lerner, J (2001) *The Money of Invention: How Venture Capital Creates New Wealth*, Boston: Harvard Business School Press.

[64] Phillippon, T and Veron, N (2008) *Financing Europe's Fast Movers*, Bruegel Policy Brief 2008/10.

On the other hand, grants can be more suitable, even for revenue generating / saving projects, where there is a need for an 'incentive effect' to persuade organisations to undertake initiatives that they would not do otherwise. They may also be more efficient where there is a small number of small-scale projects involving recipients such as social enterprises who are unused to market-based products.

Grants and financial instruments can complement one another within the same project by, for example, grant funding feasibility studies which may demonstrate the viability of support through financial instruments or through loans at subsidised rates of interest.

Debates over different forms of support have long been part of policy design discussions in the field of international development aid, and have often been controversial.[65] The debt crisis in many developing countries in the 1980s led to a reappraisal of the respective role of grants and loans in development policy. This followed the so-called Meltzer Commission report[66] which had concluded that development assistance should be administered through performance-based *grants* rather than soft loans, and that these grants should be disbursed not to governments, but rather to NGOs, charities or private sector organisations who would bid for funding.[67] The practical outcome is said to have been the establishment of 'best practice' in lending and grant awards that include elements such as debt sustainability analysis for loans or grant financing rationales for public 'goods' (such as addressing HIV or climate change).[68] At the same time, an emerging strand of thinking eschewed arguments about whether loans or grants are more suitable *per se*, but instead argued that the key issue is how to *combine* support through financial engineering mechanisms that best suit development needs.[69]

Box 2.8: What kinds of market imperfection can financial instruments address?

Financial instruments can be used to support revenue generating or saving investments where the private sector may not be willing or able to provide any or all of the capital requirements. Examples include:

- Loans to support training of individuals where the individual lacks the credit history to secure conventional finance either at all or on affordable terms
- Loans and loan guarantees for micro enterprises where transaction costs and risks are too high or too difficult for conventional private sources to appraise
- Equity investment in young firms with significant capital requirements and high risk investments
- Long-term loans for energy-efficiency investment resulting in cost savings and environmental benefits
- Mixed packages of repayable support for multi-use urban generation designed to 'crowd-in' private sector funding partly through policy 'signalling'.

In practical terms, a role for financial instruments is only feasible where the ultimate investment is ***income-generating***, enabling the initial support to be repaid. This means that where public intervention is justified by the need for public goods, repayable support

[65] It is, incidentally, evident that the controversy arises partly from the formal definition of Official Development Assistance and its use as mechanism to hold donors to account – see Hynes, W and Scott, S (2013) The Evolution of Official Development Assistance: Achievements, Criticisms and a Way Forward, OECD.

[66] IFIAC (International Financial Institutions Advisory Committee) (2000), Report of the International Financial Institution Advisory Commission ("Meltzer Report"), United States Congress, Washington, DC.

[67] Cohen, D, Jacquet, P and Reisen, H. (2007) Loans or grants? CEPR Discussion Paper Series 6024.

[68] Arvanitis, Y. (2013) Blending grants and loans for private sector development: the use of grants elements and the AfDB's experience, Africa Economic Brief, 4(2).

[69] Jacquet, P. and Severino, J-M. (2004) 'Prêter, donner: comment aider?' *Revue d'économie financière.*

is unlikely to be well-suited. In other words, appropriate forms of finance need to be tailored to the market imperfection being addressed. Three principal benefits of financial instruments opposed to grants are conventionally highlighted.[70]

First, FIs are more ***sustainable*** because funds are repaid, creating a legacy to invest again. For policymakers with long experience of financial instruments, this is often regarded as the key benefit, even if it is not always the primary consideration among newer FI practitioners.[71] Importantly, however, the scale of returns depends not only on the presence of sufficient numbers and scale of viable projects that are not commercially funded and the scope for timely exits and repayments, but also on the level of costs involved in running repayable funds and the need for defaults, losses and fees not to erode returns.

Second, FIs can improve ***project quality*** – this may be partly through the due diligence involved in private sector project assessment, but also because having to repay support focuses the recipient on the obligation to repay. This rationale is partly founded on the idea that the level of deadweight involved in FIs is lower than for grants; there is also a psychological dimension as both investee and investor share the risk, though how this is distributed will depend on how the instrument is designed. In addition, the use of FIs is influenced by the view that private sector expertise in assessing business plans improves the viability of projects compared to grants.

Third, and partly related to the sustainability argument, FIs can make more ***cost-effective*** use of public funds partly because funds may be recycled, but also because of their potential to attract private funds. This argument was particularly significant in the context of the financial crisis, which affected not only public spending but also the willingness of the private sector to lend and invest. That said, there is limited evidence of the capacity of public FIs to draw in private capital, and many ESIF co-funded instruments use public capital alone.[72] A secondary benefit related to private capital is the scope for publicly backed financial instruments to support the development of local (or sometimes larger) private financial markets.

Box 2.9: How has the financial crisis affected the justification for using financial instruments?

The financial crisis and its aftermath have increased both the scope and the need to use financial instruments in economic development policy. Public expenditure constraints have reduced the scale of funding available and intensified the requirement for financially sustainable solutions for infrastructure spending. The crisis has also affected access to finance for some businesses, especially SMEs; these tend to be more reliant on bank lending which has become more constrained as banks sought to rebuild their balance sheets.

While these benefits might be accepted as conventional wisdom, ***financial instruments are not suitable for all types of intervention***. As outlined earlier, the justifications for intervening vary and these in turn affect the choice of delivery mode (whether non-repayable or financial instruments). In practice, however, the academic and policy literature reveals little research on the relative merits of grants versus financial instruments in different situations. A recent 'think piece' posited that there should be a

[70] European Commission (2012) *Financial Instruments in Cohesion Policy*, Commission Staff Working Document, SWD (2012)36 final, Brussels 27 February 2012.

[71] Wishlade, Michie R, Familiari G, Schneidewind P and A Resch (2016) *Ex-post evaluation of Cohesion policy programmes 2007-2013, focusing on the European Regional Development Fund (ERDF) and Cohesion Fund (CF) – Work package 3: Financial instruments for enterprise support*: Final report to the European Commission.

[72] Ibid.

presumption in favour of using financial instruments in supporting SMEs, but that ***grants might be appropriate in four scenarios***: [73]

- for early stage research and development (where there is an established precedent for the provision of grants to new ventures to support proof of concept and provide seed funding, and grants may be appropriate early rounds of funding for young, small technology-based SMEs)
- to encourage change in behaviour, such as investment in energy-saving measures (using a grant to incentivise behaviour change to tackle an important market failure and to deliver public goods);
- at key points in their development, for social enterprises and charities (some of which will never be traded on markets or be financially self-sustaining); and
- addressing a viability gap to enable a project to proceed (where own contributions and commercial sources are insufficient but additionality and value for money criteria are met). In these circumstances there may be a case for grant to fill the viability gap and enable the project to go ahead, if additionality and value for money criteria are met.

The ***relationship between grants and financial instruments*** and their respective roles is rarely well articulated in policy – whether in the domestic arena or in the implementation of Cohesion policy by national and regional authorities. There is a need for the SME support offer to be coordinated (e.g. FIs will not be attractive when grants are available for similar purposes)[74] and a plethora of schemes causes confusion for recipients.[75] While this has not received much attention in the past, the recent evaluation of FI for enterprises in Cohesion policy 2007-13 suggests that this is rising up the agenda following the wider use of FIs in 2007-13. Some MAs perceived FIs as improving the capacity of Cohesion policy to meet targets, in comparison with grants,[76] with a key benefit being that FIs discourage grant dependency, promote an "entrepreneurial culture" and may support (niche) market development. Moreover, FIs require more corporate finance expertise, potentially improving sound decision-making.[77] That said, grants are often considered easier to administer.[78]

Box 2.10: Energy Efficiency: FIs v Grants – the 2007-13 Experience

Most support for energy-saving in Cohesion policy was in the form of grants; loans making up only eight percent of total commitments. A higher proportion of *domestic* funds were in the form of repayable instruments (about one-third). MAs preferred grants for several reasons, including:

- reluctance by potential applicants to engage with loans (especially in EU12 countries), due to a) constraints on public authorities taking on loan commitments (in the case of public buildings) and b) cultural reluctance to accept loan commitments (in the case of residential buildings)
- administrative complexity and limited experience in using loans or other FIs

[73] Regeneris Consulting and Old Bell 3, *Grants for SMEs in Wales* http://gov.wales/docs/wefo/publications/150127thinkpiecesmegrantsinwales.pdf

[74] Faiña A, Lopez-Rodriguez J, Montes-Solla P, and Varela Candamio L (2012) *Expert evaluation network delivering policy analysis on the performance of Cohesion Policy 2007-2013. Task 1: Financial engineering*.

[75] Evans, D J (2013) *Access to Finance Review: Stage 1 Report & Stage 2 Report*, Welsh Government.

[76] Wishlade, F, *et al* (2016) *Financial Instruments under Cohesion Policy 2007-13: How have Member States and Selected Financial Institutions Respected and Preserved EU Financial Interests?,* Report prepared for the European Parliament Committee on Budgetary Control.

[77] Regeneris Consulting and Old Bell 3, *Grants for SMEs in Wales* http://gov.wales/docs/wefo/publications/150127thinkpiecesmegrantsinwales.pdf

[78] Wishlade, F, *et al* (2016) *Op cit.*

- additional demands on target beneficiaries and in some cases significant effort required to encourage uptake.

Grants were considered to be more appropriate than FIs for: "deep energy efficiency interventions where beneficiaries may face uncertainty about the pace and scale of payback of the investment". Such projects are typically: more costly; more risky in terms of outcome (e.g. energy savings); and less attractive funded on a loan basis. Deep energy renovations imply higher costs than a traditional, usually partial, energy upgrades of buildings. Ambitious investments are needed to avoid a 'lock-in effect', where recently-renovated buildings are still not sufficiently efficient to meet policy objectives. High-profile investment in relatively new deep renovation techniques could help to stimulate a more self-sustaining market for them in future (providing a demonstration effect) and improve skills of the construction industry. The evaluation suggests that the intensity and form of support could be differentiated depending on the ambition of the energy upgrade, with higher subsidies available when more energy reduction is possible, with linked use of FIs, where appropriate. For residential buildings, a higher ratio of grant funding could be appropriate for fuel-poor home-owners, but 'channelling generous levels of support' to public buildings, could dilute the impact of ERDF/CF support and weaken the exemplar role of such investments, and make public authorities reluctant to make energy efficiency investments from own resources. Institutional constraints to the use of FIs may be present. These could be addressed by to enabling loan commitments on an "invest to save" basis, or through vehicles such as energy service companies (ESCO).

Source: Ramboll and IEEP (2015) Ex post evaluation of Cohesion policy programmes: Energy efficiency in public and residential buildings, Final Report to the European Commission.

The scope to ***combine different forms of support*** has been given limited consideration in Cohesion policy, but blending loans and grants has become common practice in international development finance.[79] This involves the combination of grant aid from official development assistance with other public or private sources of finance such as loans and risk capital. This approach is perceived to offer a number of advantages, some of which are relevant to Cohesion policy, in particular:

- the scope to do 'more with less', as already mentioned
- the possibility to ensure the uptake of international political and technical standards
- the ability to enhance 'ownership' through close involvement in the design and implementation of the funding
- the capacity to open up and provide incentives for entry into new or otherwise too risky markets for the private sector, and lever in private funds.

Potential downsides are also identified, including:

- the risk that financial incentives outweigh development objectives
- the possibility that finance becomes too concentrated on certain sectors if funding follows 'market led' trends
- ill-defined monitoring and evaluation
- inefficiencies in the way in which private investment is incentivised

Box 2.11: What are the institutional considerations concerning forms of public intervention?

Financial instruments vary widely in scope, scale and design, which in turn has significant implications for governance and administration. This too means that institutional context and capacity play an important role in determining what forms of support are workable. Partly related, the maturity of the financial intermediary market can affect the feasibility of introducing different kinds of instruments.

The spectrum of intervention in the form of financial instruments can range from measures which involve many thousands of quite standardised transactions – for example in the form of loan

[79] Bilal, S and Krätke, F (2013) Blending loans and grants for development: an effective mix for the EU? ECDPM Briefing note 55.

guarantee schemes to SMEs – to measures comprising of only a few operations and involving complex arrangements and compliance issues – like urban development programmes. To this extent it is difficult to generalise on institutional issues, except to note that *context matters*.

Financial instruments have the potential partially to compensate for weak public administrative capacity – for example by using market-based measures in the form of soft loans administered by banks, as opposed to grant schemes managed by public authorities. Public financial instruments may therefore 'piggy back' on existing mechanisms offered through national promotional banks or the retail banking sector to provide an additional 'tranche' of funding, with conditions adjusted to reflect policy objectives.

Conversely, publicly-backed financial instruments can also help develop weak financial markets – for example through co-financing schemes that, in the long term, help draw in and expand business angel networks or regional venture capital markets. At the same time, certain types of financial instrument may be difficult to deploy because of so-called 'market thinness' and the absence of a well-developed pipeline of investible projects requiring wider forms of intervention to develop the necessary critical mass.

In considering forms of intervention and rationales for FIs, it is important to stress that ***the term 'financial instrument' encompasses very diverse financial products*** that differ considerably in terms of their suitability for different targets, their implications for recipients and their modes of governance, among other things; in short, the common denominator is simply that funding is repayable. The conventional breakdown distinguishes loans, guarantees and equity, but there are a number of variants and the possibility of combining one or more product to meet the needs of both the funder and the final recipient. The various forms also carry advantages and disadvantages for recipients and policymakers.

Box 2.12: What are the roles of different financial products?

Although often discussed collectively, financial instruments comprise very diverse products: they fulfil different functions for final recipients and have different implications for policymakers and financial intermediaries.

Guarantees are arguably the most straightforward to design, implement and to recalibrate as economic development needs change. They have most potential for impact where collateral-based lending is the norm and the business population is not asset rich. The use of guarantees (in domestic and Cohesion policy) is significant in only a few countries, and the sums covered are, on average often modest, partly because they are frequently combined with loans in microfinance packages for start-ups and young firms. However, where they are used, their reach can be significant, with many thousands of publicly-backed guarantees offered annually in some countries.

Loans are the most widely used source of private finance for SMEs and are offered almost everywhere in domestic and / or cofinanced economic development policies; loans are also widely used by other project promoters, such as local authorities for capital investment. Loans are comparatively easy to administer from a public administration perspective to the extent that the implementation of a loan fund can be 'outsourced' or funds can essentially be used to increase the volume of finance available through existing commercial sources. Loan products can help address credit rationing, as well as cost-of-credit issues (through interest rate subsidies or easier terms). Loans are typically preferred by some SMEs because there is no loss of control or ownership, as with equity, but they can lack the flexibility required by young firms.

Private equity markets vary widely across Europe and equity and venture capital are not prominent sources of finance for SMEs, especially smaller ones. Indeed, across Europe, over 80 percent of SMEs consider that 'equity is not applicable to my firm'[1]. Publicly-backed equity is the least-used of the three 'conventionally-defined' financial products and is often regarded as a 'niche' product for potentially fast-growing innovative firms. Equity products can provide significant amounts of medium-to-long-term capital, but imply at least some loss of management control by founders and are typically more difficult to manage for public authorities.

[1] European Commission (2013) SME Access to Finance Survey

Loans are the most widely used and simple form of support. The terms of the loans can vary widely with respect to: interest rate, coverage, duration, collateral requirements, and so on. There are a number of ***advantages to loan instruments***:[80]

- Firms may prefer debt to equity due to the lower information and dilution costs.[81]
- There is no loss of control over how the business is managed.
- The amount of capital and interest are known amounts that can be factored into business planning.
- The interest rates can incorporate a subsidised element so that the loan is offered below market rates.
- For MAs and intermediaries, loans are relatively easy to administer and the State aid compatibility is straightforward even if a subsidy element is incorporated.
- Returns to the fund should be quite predictable.

Disadvantages to loan instruments can also be identified:[82]

- Loans may lack flexibility; they must be repaid on a fixed timescale and the burden of repayments may affect cash flow and/or the capacity of the firm to expand.
- Changes in market conditions can affect the ability of the firm to repay the loan.
- Collateral might be required, this can involve debt being secured on property or guarantees, for which further payment is required.
- For MAs and intermediaries, the key disadvantages are:
    - a capital outlay is required at the outset
    - returns may be unpredictable.
    - Loans funded through Cohesion policy may be either crowding-out private investment or investing in projects which the private sector has, for sound reasons, rejected.
    - There may be administrative complexities around the management and re-use of loan repayments.

Guarantee funds provide support to companies unable to obtain finance, typically debt finance, due to a lack of collateral. Guarantee funds (and cross or counter-guarantee funds that provide support to intermediaries providing guarantee funds) are an important source of support for new businesses. There are a number of ***advantages to guarantees***:[83]

- They are relatively simple to design and administer and typically require investment appraisal to be conducted on a commercial basis, minimising deadweight.[84]
- They have the most potential for high and positive effects in countries and regions where collateral-based lending is the norm and where the entrepreneurial population is not asset-rich.[85]
- Appropriately designed, they provide access to finance that would not be available otherwise, and sometimes more cheaply as a result of the guarantee.

[80] Michie R, Wishlade F and Granqvist K (2013) Financial Instruments for Business Development in EU Cohesion Policy: National Experiences, Issues and Options. Report to Lombardy Region on the 2007-13 Operational Programme, European Policies Research Centre, Glasgow; Schneidewind *et al*. (2013) *Op cit*.

[81] Rigby J and Ramlogan R (2013) Access to Finance: Impacts of Publicly Supported Venture Capital and Loan Guarantees, NESTA Working Paper No. 13/02.

[82] Michie R, Wishlade F and Granqvist K (2013) *Op cit.*

[83] *Ibid*.

[84] Cowling M (2012) Credit rationing, equity gaps and policy solutions for financing entrepreneurial business in Europe: Theory, tests, evidence and the design and effectiveness of policy instruments, report to European Commission.

[85] *Ibid*.

- For managing authorities and financial intermediaries, guarantees require less capital outlay. In addition, State aid clearance is relatively easy, especially if the country concerned has an approved formula for calculating the aid element.
- Guarantees can also be useful in addressing credit rationing, for example: where the banking sector is highly concentrated and there is a lack of 'relationship' banking; where commercial loans require assets to be placed as security; where there is a diverse entrepreneurial population (poor as well as rich entrepreneurs); where there is substantial diversity in the quality of lending institutions; and where access to loans is conditional on factors not related to project quality.
- Evidence suggests that access to credit is of greater concern to firms than the cost of credit, implying that loan guarantees might be a more appropriate policy instrument than soft loans.
- Can be a particularly cost effective way of creating additional employment.[86]
- Easing access to finance for credit-constrained SMEs, through schemes such as loan guarantees, provides support for important agents in the regeneration of deprived areas and businesses who are employers of under-represented groups in the labour market.[87]

A number of **disadvantages** have also been highlighted:[88]

- Guarantees can be costly and there may be no reduction in interest rates in relation to the market rate.
- The disadvantages of loans also apply to guarantees.
- For MAs/intermediaries, the 'additionality' of guarantees may be difficult to determine.[89]
- It is impossible to measure the counterfactual.[90]
- The use of guarantees requires clarity of objectives – is it to encourage lending to riskier projects, which would entail higher levels of default? Who should assess the level of risk?
- From a ESI Fund financial management perspective, a further disadvantage is the unpredictability of claims on the guarantee, making the full costs difficult to determine.[91]
- The relationship between loan guarantees and innovation is opaque and the literature is divided on whether publically funded loan guarantee schemes are effective instruments for promoting lending to SMEs.[92]

Although the co-funding of ***equity*** instruments by the public sector has gained a higher profile in recent years, equity instruments have been less widely used than other forms

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[86] Cowling M (2010) *Economic Evaluation of the Small Firms Loan Guarantee (SFLG) Scheme*, Report to BIS, Department for Business, Innovation and Skills.

[87] *Ibid*.

[88] Michie R, Wishlade F and Granqvist K (2013) *Op cit*.

[89] Guarantees may be covering bank loans that lenders would have offered anyway: one study outlines a framework of Type 1 and Type 2 errors: if a loan guarantee scheme secures a loan for a firm that later fails, this is a Type 1 error because banks made the correct decision not to lend to the firm in the absence of a loan guarantee, whereas government-backed loans which are successfully repaid would, in the absence of a guarantee scheme, represent a missed opportunity for the bank. This would be a Type 2 error' – see Astebro T and Bernhardt E (2003) The winners curse of human capital. Small Business Economics, 24. 1-16.

[90] Rigby and Ramlogan (2013) *Op cit*.

[91] For other forms of FI, there must be a capital outlay at the start and funds can be allocated until they are exhausted; for guarantees, a claim is only made on the funds if there is a default on the loan, making it more difficult to assess whether the budget limit is likely to be reached and potentially less likely that the entire amount allocated is actually spent.

[92] Rigby and Ramlogan (2013) *Op cit*.

of FI under Structural Funds programmes. Equity investment represented a comparatively small proportion of co-financed FIs in 2007-13. Some key ***advantages*** of equity include:[93]

- Equity instruments can add economic value added when designed appropriately and used in a relevant context.[94]
- Equity finance is primarily suited to firms that have high growth potential but lack the cash-flow necessary to borrow from conventional sources. From the perspective of the managing authority or investor, equity investment has the potential to generate substantial returns through what may turn out to be investment in high-growth enterprises.
- The capital input may be very substantial, and it does not have to be repaid (although an entrepreneur may ultimately opt to buy-out an investor in order to regain total control of the firm).
- The investor may also bring considerable skills, experience and contacts that can support the development of the firm.
- For public investors, an equity-type instrument can provide a higher level of management control, through higher involvement of the fund in project management or the management of target companies.
- Mezzanine finance may be attractive to small firms which are resistant to pure equity.

There are also potential ***disadvantages of equity instruments***:

- Equity investment is a highly specialised form of finance and is only appropriate for a very small minority of firms.[95]
- Equity investors are purchasing part ownership, so there will be partial loss of management control of the firm. (However, although this may be a disadvantage for an entrepreneur, it could potentially be an advantage for the public investor.)
- The main issues to arise in the design of equity instruments using ESI Funds relate to their complexity:[96]
    - Difficult State aid issues may arise depending on the type and scale of investment targeted.
    - Management costs may be high, partly owing to the due diligence to be carried out.
    - It may prove difficult to lever in private sector investment.
    - Returns are unpredictable both in terms of scale and timing and depend on the capacity to exit the investment.
- These instruments are less successful in regions and countries where the innovation infrastructure and ecosystem is not developed enough to support and sustain the creation of knowledge that can be commercialised.[97]
- Access to venture capital is very dependent on proximity of venture capital firms and urban centres.[98]
- There is evidence of poor performance where funds are geographically constrained.[99]

As already noted, the three main types of financial product have many variants. Moreover, beyond ESI Fund policies, an array of complex financial mechanisms is in evidence in international development policy, domestic financing of public investment

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[93] Michie R, Wishlade F and Granqvist K (2013) Op cit; Schneidewind P, et al *Op cit*.

[94] Cowling M (2012) *Op cit*.

[95] Ibid.

[96] Michie R, Wishlade F and Granqvist K (2013) *Op cit*.

[97] Cowling (2012) *Ibid*.

[98] Rigby J and Ramlogan R (2013) Op cit.

[99] Ibid.

and through the Investment Plan for Europe and other EU level initiatives, especially those supported by the EIB Group. These include various forms of structured finance, securitisation and public-private partnerships.

Arguably the key issue to emerge from the above discussion is ***the importance tailoring the financial product appropriately***. Financial instruments within the ambit of Cohesion policy in 2007-13 concerned support for enterprises (principally SMEs), urban development and energy efficiency. In 2014-20, financial instruments can be used for any of the Thematic Objectives, though TO3 (SMEs) and TO4 (low carbon), and especially the former, are likely to dominate in the use of financial instruments. ***Different types of market imperfection give rise to different funding constraints and solutions,*** as summarised in Figure 2.12.

Figure 2.12: Target recipients, market imperfections and rationales for FI

Source: EPRC compilation.

2.3.3. What is the rationale for Cohesion policy to co-finance FIs?

The final, rather narrower, sub-question concerns the rationale for Cohesion policy co-financing of financial instruments. Clearly, arguments for financial instruments – namely sustainability, project quality and efficiency – all play a role. However, as the ex post evaluation of financial instruments for SMEs[100] showed, countries and regions took very diverse approaches to the use of financial instruments in Cohesion policy in 2007-13. There are few clear patterns underpinning this, but key considerations include:

- The objectives of the OP and whether these are capable of being addressed through financial instruments – for OPs with small financial allocations, the aims are often narrowly focused and may not be susceptible to the use of FIs.
- Small size of the financial allocation. In some cases this underpins a decision *not* to use FIs partly owing to the relatively onerous administration and governance involved, and the lack of 'critical mass' (as in Flanders, BE); conversely, the small allocation may be regarded as an opportunity to focus resources and create sustainable funds (as in London, UK).
- The role of domestic sources of FI. For some countries with longstanding domestic FIs, co-funding may simply complement those resources, providing a supplementary 'block' of finance administered alongside domestic funds, typically by entrusted institutions with long experience (as in some German *Länder* and Wallonia (BE)).
- The opportunity to experiment with forms of finance not widely used previously.

In short, there are various motivations for co-funding FIs, but these are very much context-driven, reflecting the scale and focus of OPs, the appetite to experiment with forms of finance not widely used in domestic policy, as well as the wider domestic financial context.

In 2014-20, the picture has become more complex in two main ways. First, financial instruments can be used across all policy areas, opening up new possibilities for ways of funding programmes, but also the prospect of applying already complex financial products to activities in which there is limited experience. Second, the decline in public investment and the need to reignite growth in the European economy have prompted the emergence of a range of 'sectoral' initiative in areas that potentially overlap with the objectives of the ESI Funds. Tasks 4 and 5 of this study explore the impact of this new environment in practice.

2.4. What evidence is there of the *effectiveness* of co-funded FIs?

The 'effectiveness' of co-funded FIs concerns their contribution ***to achieving OP objectives.*** However, FI *performance* goes beyond the programmed results and targets to embrace disbursement rates, private sector leverage effects and the generation of returns and value for money.

While the literature on repayable assistance is expanding, ***evaluation evidence of the effectiveness of co-funded FIs remains limited***. What does exist is overwhelmingly orientated towards enterprise support and the different dimensions of the 'access to finance' question. As such, urban regeneration and energy efficiency FIs along with repayable measures under ESF and EMFF receive considerably less attention, reflective of the relative lack of experience and lower uptake of repayable assistance in these areas. More specifically, much of the wider (i.e. non Cohesion policy) literature focuses on publicly backed venture capital. However, this is the least used of the three main types of financial instrument co-financed through the Structural Funds. Furthermore, although recent attention has focused on the availability of equity, largely owing to its perceived

[100] Wishlade, Michie R, Familiari G, Schneidewind P and A Resch (2016) *Op cit.*

role in financing potentially high growth enterprises, many EU countries have long traditions of providing soft loans and or guarantees as instruments of national or regional economic development policy. However, these instruments appear to be relatively under-evaluated, particularly in countries without a strong tradition of regular policy reappraisal. Last, and as mentioned above, few studies consider the rationale for the form of intervention – grants as opposed to repayable mechanisms – or the relative efficiency of public funds disbursed in repayable form and their capacity to draw in private funding; these issues are mentioned in some studies, but are not the primary focus of any of those identified in the literature search.

Managing authorities report FI data regularly to the Commission, as part of the Annual Implementation Report process. However, there are a number of issues with the quality and reliability of this data, further complicated by the fact that reporting requirements for many indicators were voluntary in 2007-13. Despite this, ***there is some evidence of FIs having helped achieve OP objectives***. The recent ex-post evaluation of FIs for enterprise support shows that, for the OPs analysed, almost all of the Priority Axes where FIs were implemented met their operational objectives, 70 percent achieving them to a high degree.[101] FIs were found to have clearly improved access to finance for a considerable number of enterprises in case study OPs (e.g. around 7 percent of all SMEs in Lithuania) - accordingly, an important OP objective, to ´increase SME access to finance´, was achieved. However, data was too poor to assess the contribution of FIs in terms of final outcomes such as productivity, jobs created etc. as too few MAs provided such data related to FIs to make any assessment of their impact. However, the flexibility of FIs was valued – relating to the capability of FIs to offer a wider range of financing needs and allow firms to access funds for working capital, which in times of crisis was often what SMEs required rather than finance for further investment.[102]

In terms of revolving funds and the ***ability of FIs to create 'legacy'***, perhaps the main rationale for using FIs in place of grants in Cohesion policy programmes, there is again little evidence on the level of returns being achieved so far by co-funded FIs. The 'revolving' aspect of FIs has been treated very differently among different Member States and regions, and many FIs lacked an explicit strategy for revolving funds or providing a legacy.[103] Data has been found to be too thin and too unreliable to make even tentative estimates of 'revolved' public money. The ex post evaluation reported that loan schemes in five case study OPs (out of nine case studies carried out) had reported revolved money – with a range of between 25 percent and 200 percent of the original amount disbursed. Other loan schemes had not yet reached the stage of revolving, partly due to the late start and the average loan duration. Similarly, most venture capital FIs were established for a fixed duration, typically 10 years, and so the final financial outcome and hence the sustainability of the public money invested had not been estimated.

The potential ***attraction of additional private sector investment*** is another reason given by the Commission and Managing Authorities for co-funding FIs in Cohesion policy. The ex-post evaluation of FIs for enterprise support found that only just over five percent of funds paid to holding funds and specific funds came from private sources. However, this varied widely between countries, with the UK, FR and PT attracting private finance but other Member States attracting none. Levels of private sector participation also differed significantly between the types of FIs, with co-funded guarantee schemes attracting high leverage rates, and a mixed picture for equity.[104] A report for the European Parliament found that although the majority of (Managing Authority)

[101] Ibid.

[102] Ibid.

[103] Ibid.

[104] Ibid.

interviewees considered that they had been very successful in attracting private finance under their FIs, hard data was difficult to obtain and interpret.[105] However, the potential of FIs to help develop private investment has been viewed positively, and there is evidence that ERDF support has helped the creation of a venture capital market in some areas where it was poorly developed.

On the ***cost-effectiveness*** of co-funded FIs, there is limited evidence to demonstrate whether or not FIs represent better value for money than grants. In the Czech Republic, FIs were found to be more cost effective than grants when it came to creating jobs, while in Bavaria the opposite was found to be true.[106]

In terms of evaluations of specific types of FIs, ***co-funded soft loans and interest-rate subsidies may be more cost-effective*** in creating employment and boosting sales for many SMEs in certain circumstances, outperforming grants. However, grants were found to be more suitable for small firms who are in need of smaller amounts of finance, which would not be provided by private debt finance.[107] Co-funded FIs also outperformed grants under an ESF measure to fund start-ups.[108] While grants remained unsurprisingly much more popular, the loans offered to individuals were considered more effective as they discouraged those who had not fully considered the viability of their plans.

Box 2.13: Effectiveness of FIs for urban development and energy efficiency

In 2007-13, co-funded FIs could be used for enterprise support, or for urban development or energy efficiency. Most evaluations focus on FIs for enterprise support, reflecting lower usage of FIs for urban development or energy efficiency, and the fact that many of these FIs were introduced later in the programming period. The majority of existing literature on JESSICA urban development FIs, for example, takes the form of EIB-commissioned feasibility studies, seeking to determine the correct scale and model for implementation, providing no ex post evidence on effectiveness. The long-term nature of the investments made under JESSICA-type FIs implies that more literature will emerge over coming years.

Financial instruments have limitations, for example where a lack of subsidies means that new enterprises are less willing to initiate the early stage of innovation, where high management costs are involved, or where results are disappointing – for instance if the funds are not achieving the expected returns and are becoming more conservative in their investments with the result that they cannot be differentiated from 'ordinary' investors.[109]Another limitation (also potentially true of grants) is the possibility that co-funded FIs crowd-out private sector finance. One study questioned the strategic value of (co-funded) subsidised loans, as positive effects were found to be negligible or non-existent, while the potential for crowding-out of local banks was too high. In addition, commercial banks risked becoming too accustomed to the risk cover provided via

[105] Wishlade F, et al (2016*) Op cit*.

[106] Wishlade, Michie R, Familiari G, Schneidewind P and A Resch (2016) *Op cit*.

[107] Bondonio, D and Martini, A (2012) *Counterfactual Impact of the Cohesion Policy: Impact and Cost Effectiveness of Investment Subsidies in Italy*, Final Report to DG Regional Policy.

[108] Zub, M, *et al* (2015*) Badanie Skuteczności Wsparcia Realizowanego W Ramach Komponentu Regionalnego Po Kl 2007-2013/* Study (The Effectiveness of Support Provided under the Regional Component of the Human Capital OP 2007-2013), Ministry of Regional Development, Poland.

[109] Bodewes Beleidsadvies (2014) Regionale Activiteiten en Investeringen Gericht op R&D en Innovatie.

ERDF.[110] These limitations point to the need for financial instruments to be carefully designed to address specific needs and tailored to context.

Evidence suggests that FIs ***are most effective where tailored to specific regional or national circumstances***, as there is no successful 'one size fits all' approach for FIs, and models are seldom transferable without modification to take local, regional or national circumstances into account. This can include differences in local economic conditions, in banking and legal systems, previous experience with implementation of FIs etc. Several academic papers emphasise the need for instruments to be tailor-made for different areas.[111] External framework conditions play an important role in access to finance and must be taken into consideration as a significant part of the policy mix.[112] In some cases this may require significant domestic legislative change – as was required in France in order for the relevant regional authorities to have the legal competence to operate JEREMIE-type funds.[113]

Preliminary gap assessment or market analysis before setting up co-funded FIs was not mandatory until the 2014-20 period, and was not always carried out. In some cases this contributed to over-capitalisation of FIs, or poor targeting[114], suggesting that ***FIs are most effective where they are based on an accurate assessment of the market situation***, providing clear evidence for government intervention. Research on market gaps and economic structures is key to accurate instrument design and funds allocation, as market conditions are diverse.[115]

Managing authorities have highlighted that the ***effectiveness of FIs improves where there is flexibility and an ability to respond to change***. The EIB's stocktaking report found that most Managing Authorities in 2007-13 had to deviate from their initial plans due to changing circumstances.[116] The need to adapt to change has implications for the ex ante assessment, which should be reviewed regularly to check economic circumstances and market needs. Implementation structures chosen must ensure flexibility is possible; monitoring has an important role to play in providing feedback on performance. For example, *Investitionsbank Berlin* (DE) works in partnership with a local credit research company which conducts interviews with 1,000 SMEs in Berlin each year. These interviews assess the ease of access to debt finance and the extent to which companies use public finance. The results of this survey are then used to evaluate, improve or adjust FIs.[117] In terms of flexibility in implementation structures, holding

[110] Hyytinen A & Ylhäinen I (2012) Julkisen yritysrahoituksen vaikuttavuus: Esimerkkinä erityisrahoitusyhtiö Finnvera, In Työ- ja elinkeinoministeriö Kasvuyrityskatsaus 2012, Työ- ja elinkeinoministeriön julkaisuja. Innovaatio 20/2012.

[111] Veugelers R (2011) *Op. cit*.; Tykvová T, Borell M and Kroencke TA (2012) *Potential of Venture Capital in the European Union*, European Parliament, Directorate-General for Internal Policies; Berggren, B and Silver, L (2012), *Op. cit*.

[112] OECD (2009) *Policies for Seed and Early Stage Finance: Findings from the 2012 OECD Financing Questionnaire*, OECD Science, Technology and Industry Policy Papers, No. 9.

[113] Michie R and Wishlade F (2011) *Between Scylla and Charybdis: Navigating FIs through Structural Fund and State Aid requirements*, IQ-Net Thematic Paper No. 29(2), EPRC, Glasgow.

[114] Wishlade, Michie R, Familiari G, Schneidewind P and A Resch (2016) Op cit.

[115] Cowling, M. (2012) Op cit.

[116] Van Ginkel J, Vyas L, Cairns R, Michie R, Granqvist K and Atkinson S (2013), *Financial Instruments. A Stocktaking Exercise in preparation for the 2014-2020 Programming Period – Report to EIB.*.

[117] Michie R, Wishlade F and Gloazzo C (2014) *Guidelines for the Implementation of Financial Instruments: Building on FIN-EN,* Final report to Finlombarda SpA.

funds/fund of funds models can provide the ability to move resources between funds depending on demand, although they bring an additional tier of costs.[118]

FIs are most effective where there are safeguards against 'objective drift', ensuring investments are in line with the strategies and targets set. Private sector management of publically funded FIs brings additional challenges. An evaluation of ERDF-funded venture capital and loan funds carried out for the Commission in 2007 points out that the extent of public or private involvement in venture capital and loan funds can have implications for risk management and the relative emphasis on regional development objectives versus purely financial objectives.[119] Evidence from the evaluation suggests that public sector involvement leads to a greater focus on purely regional development objectives. Also, because the public sector shareholders perceive the impact on regional development as one of the most important aims of venture capital and loan fund interventions, they are often willing to assume greater risks and accept lower financial returns. This can increase deal flow and widen the impact on jobs. In contrast, private shareholders are likely to be more concerned with financial returns and see regional development impacts more in terms of the 'demonstration effect' arising from a professionally managed venture capital operation. Monitoring and evaluation have an important role to play here – as do the business plan, funding agreement and contractual arrangements - in maintaining a close link between policy objectives and outcomes.[120]

FIs have been ***most effective where they build on previous experience*** in the region/Member State. Creation of successful FIs is an iterative process, involving trial and error. In Nordrhein-Westfalen, for example, when co-funding FIs under the ERDF OP in 2007-13, it was considered appropriate to draw on the existing expertise and structures within the NRW *Land*-owned public investment bank, NRW.BANK, rather than setting up a parallel institutional framework. It was also hoped that the use of the *Land* Investment Bank would ensure that the fund was fully neutral and would not favour any particular lending institutions. The perceived advantages of the *Land* Investment Bank are its familiarity with the financial circumstances of local firms and its experience in working closely and constructively with the different *Land* Ministries and playing a bridging role between the *Land* government, commercial/cooperative banks and local SMEs.[121]

Whether support is provided in the form of grants or FIs, effectiveness will depend on whether the ***aid is well-focused and related to the programme strategy***. For example, DG REGIO's expert evaluation network reports on financial instruments noted that in Austria, Belgium and Sweden FIs and grants were considered complementary in 2007-13 OPs and formed different components of a strong policy support offer.[122] Equity in particular was considered less successful where the business support environment and support infrastructure is underdeveloped, and in general, more preparation and

[118] Ibid.

[119] CSES (2007) *Comparative Study of Venture Capital and Loan Funds Supported by the Structural Funds*, Final Report, August 2007.

[120] Wilson, K and Silva, F (2013) Op cit.; NEA2F (2013) *North East Access to Finance: The Future Shape of Access to Finance: Strategic Overview and Recommendations*.

[121] Michie R and Wishlade F (2011) *Op cit*.

[122] Resch A and Naylon I (2012) *Financial engineering: Austria 2007-13*, report to European Commission; Greunz L (2012) *Financial engineering: Belgium 2007-13*, report to European Commission; Nilsson J-E, (2012) *Financial engineering: Sweden 2007-13*, report to European Commission.

awareness is needed for SMEs with regard to equity.[123] Demand side policies to develop entrepreneurial and investment talent and networks are also critical and there is a strong need for provision of information, advice and hands-on support.[124] This is linked to coordination between different government departments and links with the private sector. This in turn puts a premium on the need for capacity-building, a key conclusion of the 2013 stocktaking report.[125]

[123] Cowling M (2012) Op cit.; Baldock R and North D (2012) *The Role of UK Government Equity Funds in Addressing the Finance Gap facing SMEs with Growth Potential*, Paper for the Institute for Small Business and Entrepreneurship Conference, 7-8 November, Dublin.

[124] Wilson, K and Silva, F (2013) Op cit.; NEA2F (2013) *North East Access to Finance: The Future Shape of Access to Finance: Strategic Overview and Recommendations*.

[125] Van Ginkel et al (2013) Op cit.

3. THE USE OF FINANCIAL INSTRUMENTS CO-FINANCED BY ERDF, COHESION FUND, ESF AND EMFF IN 2014-20

Key findings

- Member States planned to almost double spend on financial instruments in 2014-20 compared to 2007-13.
- Plans vary very widely with four Member States planning to commit more than four times 2007-13 levels (NL, PT, RO, SI), and others planning to reduce or even cease using FIs.
- Some plan to commit more than 8 percent of OP contributions in the form of FI (BG, HU, LT, NL, PT, SI, UK).
- Planned FI allocations remain predominantly under ERDF, but usage of the ESF and EMFF has also increased.
- The primary focus of FIs is on SME competitiveness, but support for research and innovation and low carbon is also significant.
- Around half of all OPs (except Interreg programmes) allocate funds for FI. Some 14 OPs have planned spend exceeding €400m; collectively these account for 55 percent of planned FI spend.
- 27 OPs plan to allocate more than 20 percent of resources to FIs.
- Approaches to ex ante assessments have been very varied, with some subject to revision; plans remain in a state of flux, with some increases and some reductions in planned FI spend.
- Progress with implementation has been slow – around 23 of the 160 OP planning FIs had operational funds by spring 2016.

The overall ***objective*** of this section is to provide an overview of the rationale for, and intended use of, financial instruments in 2014-20. In gathering, analysing and presenting this information, this ***aims*** to:

- take account of the specific nature of each of the funds: ERDF, Cohesion Fund, ESF, EMFF;
- analyse information at the level of the programme, Member State, Fund, Thematic Objective and final recipient targeted;
- detail the use of FIs by key Investment Area;
- provide an overview of the main groups targeted; and
- take account of the specificities of each Fund and, where relevant, draw comparisons between 2007-13 and anticipated use in 2014-20.

The data gathering for this task drew on a number of ***sources***, specifically:

- ***Data from each Operational Programme*** (SFC data) on forms of finance and Thematic Objectives at the level of programme priorities; this data was provided by the European Commission for the ERDF, CF and ESF. For the EMFF, an initial scoping study produced under the aegis of *fi-compass* provides some initial insights into Managing Authority plans for FIs.[126]
- ***Data from DG Regio FI survey*** of planned spend and progress on FI implementation at the level of each OP, undertaken in spring 2015.

[126] Fi-compass (2015) Scoping study for the use of financial instruments under the EMFF and related advisory support activities, Final Report, June 2015: https://www.fi-compass.eu/sites/default/files/publications/EMFF_SCOPING_STUDY.pdf

- ***Excel-based fiches*** completed for each Priority Axis where financial instruments are now planned, in order to give a detailed update on actual plans for financial instruments and progress with ex ante assessments; this information was compiled on the basis of desk research by national experts.
- ***Structured descriptive information*** on financial instruments in each Member State outlining the approach to and progress with financial instruments; this information was compiled on the basis of desk research by national experts. This was based on documentary analysis and also involved the collection of relevant documentation, including ex ante assessments and evaluations.
- ***A two-part online survey*** of all Managing Authorities of ERDF, CF, ESF and EMFF programmes conducted in 24 languages with Part I to be completed by all respondents and Part II by those introducing financial instruments.
- ***Data on financial instruments in 2007-13***, based on information reported by Managing Authorities and collated by the European Commission.[127]

Figure 3.1: Summary of data sources

Source	Unit of analysis	Scope
SFC data (European Commission)	Priority Axis and below	ERDF CF ESF
DG Regio FI Unit survey (DG Regio)	Operational Programme	ERDF CF ESF
Excel fiches (EPRC national experts)	Priority axis and below	ERDF CF ESF
Structured descriptive information (EPRC national experts)	Member State and OPs planning use of financial instruments	ERDF CF ESF EMFF
Online survey Part I (managing authorities)	Operational Programme	ERDF CF ESF EMFF
Online survey Part II (managing authorities)	Funds of funds (FoF), and funds within or outside FoF	ERDF CF ESF EMFF
2007-13 Summary report (assembled by European Commission from managing authority data in AIR)	Holding funds, and funds within or outside HF	ESF and ERDF

Source: EPRC

A significant ***challenge*** in working with these different data sources is that not all are complete or necessarily easy to reconcile with one another. For example, DG Regio's survey of Member States in 2015 already showed some departure from OP plans. Also, in some cases, the Excel fiches compiled by the national experts made clear that some provisions for financial instruments in the OPs were merely tentative, or that a Managing Authority proposed to use financial instruments for a priority that was not originally planned in the OP. At the same time, approaches to financial instruments are to some extent in a state of flux, with many ex ante assessments planned, underway or completed, but with very few financial instruments actually operational.

The aim of the ***survey*** of Managing Authorities was to complement the work of the national experts (which involved a comprehensive review of the situation at the level of programme Priority Axes) with information on financial instruments at the level of each OP. While the response rate to the online survey was good overall (and exceptional in some cases) – see Figure 3.2 - inevitably not all Managing Authorities responded, so

[127] European Commission (2015) Summary of data on the progress made in financing and implementing financial engineering instruments – 2014, http://ec.europa.eu/regional_policy/en/information/publications/reports/2015/summary-of-data-on-the-progress-made-in-financing-and-implementing-financial-engineering-instruments-2014.

direct information on the current status of financial instruments remains incomplete. That said, responses were received from all Member States, with the exception of Cyprus.

Figure 3.2: Responses to online Managing Authority survey (by Member State)

Member State	Total	Non-respondents	Responses	Response rate (%)
AT	3		3	100.0
BE	8	2	6	75.0
BG	9	6	3	33.3
CY	3	3		0.0
CZ	8	1	7	87.5
DE	33	10	23	69.7
DK	3	2	1	33.3
EE	2		2	100.0
ES	45	31	14	31.1
FI	4	2	2	50.0
FR	40	28	12	30.0
GR	18	14	4	22.2
HR	3	2	1	33.3
HU	8	4	4	50.0
IE	4	2	2	50.0
IT	52	35	17	32.7
LT	2	1	1	50.0
LU	2		2	100.0
LV	2		2	100.0
MT	4	2	2	50.0
NL	6	4	2	33.3
PL	22	1	21	95.5
PT	12	4	8	66.7
RO	7	3	4	57.1
SE	12	10	2	16.7
SI	2		2	100.0
SK	7	5	2	28.6
UK	13	4	9	69.2
Interreg	72	33	39	54.2
Total	**406**	**209**	**197**	48.5

Source: EPRC online survey.

The overall response rate to the survey was 48.5 percent of Managing Authorities. However, the rate was higher (51.3 percent) among those MAs that had planned to use FIs, as indicated in the Operational Programmes. This likely represented a presumption that the survey was more relevant to MAs that intended to use FIs, although the introductory letter emphasised that 'non-user' views were also relevant. Importantly, the survey elicited a high response rate among MAs that planned significant spend of FIs. Indeed, respondents to the survey account for over 70 percent of planned spend – see Figure 3.3.

Figure 3.3: Responses to online Managing Authority survey (by users and non-users of FI)

	Number of OPs	%	Plan to use FI	%	FI total in OP €m	% of planned FI spend
Non-respondents	209	51.5	78	48.8	6209.6	29.1
Survey respondents	*197*	*48.5*	*82*	*51.3*	*15107.6*	*70.9*
Total	**406**	**100.0**	**160**	**100.0**	**21317.2**	**100.0**

Source: EPRC online survey.

The respondents also provide a good representation of financial instruments by Thematic Objective, both in terms of numbers of OPs and spend, as illustrated in Figure 3.4.

Figure 3.4: Responses to Managing Authority survey (by TO among users of FIs)

	Total planned FI spend	Planned spend by respondents	% of total	No of OPs with planned FI spend	No. of respondents with planned FI spend	% of total
TO1	3668	2667	73	68	34	50
TO2	468	404	86	5	2	40
TO3	11320	7694	68	127	65	51
TO4	3748	2610	70	79	47	59
TO5	21	21	100	1	1	100
TO6	1089	738	68	22	15	68
TO7	190	190	100	3	3	100
TO8	569	278	49	31	20	65
TO9	451	388	86	21	15	71
TO10	62	62	100	4	3	75
TO11	8	0	0	1	0	0
TO99	71	57	80	3	2	67

Note: TO99 refers to multi-thematic objectives, that is Priority Axes which address more than TO.
Source: EPRC online survey.

The discussion that follows explores this from various perspectives, providing an overview of trends in relation to 2007-13, including analyses by Member State, Thematic Objective and Investment Area, Fund, rationale and Operational Programme.

3.1. What are the overall trends in the planned use of financial instruments?

In 2007-13, Member States committed OP contributions of around €17 billion to financial instruments, of which €11.4 billion in Structural Fund resources. Indications from 2014-20 OPs are that Member States ***planned to almost double the EU amount to around €21 billion.*** Comparisons between countries and time periods are not straightforward since total EU amounts vary very widely - and in some countries these have increased while elsewhere they have declined or remained stable.[128] Nevertheless, it is useful to consider whether financial instruments are planned to become more or less important in the 2014-20 funding period, compared to 2007-13.

Member State plans should be treated with some caution since the experience in 2007-13 showed that only around 94 percent of OP contributions committed were actually paid to financial instruments,[129] but Figure 3.5 suggests that ***in most countries financial instruments will become more important***, though this is not universal. More specifically:

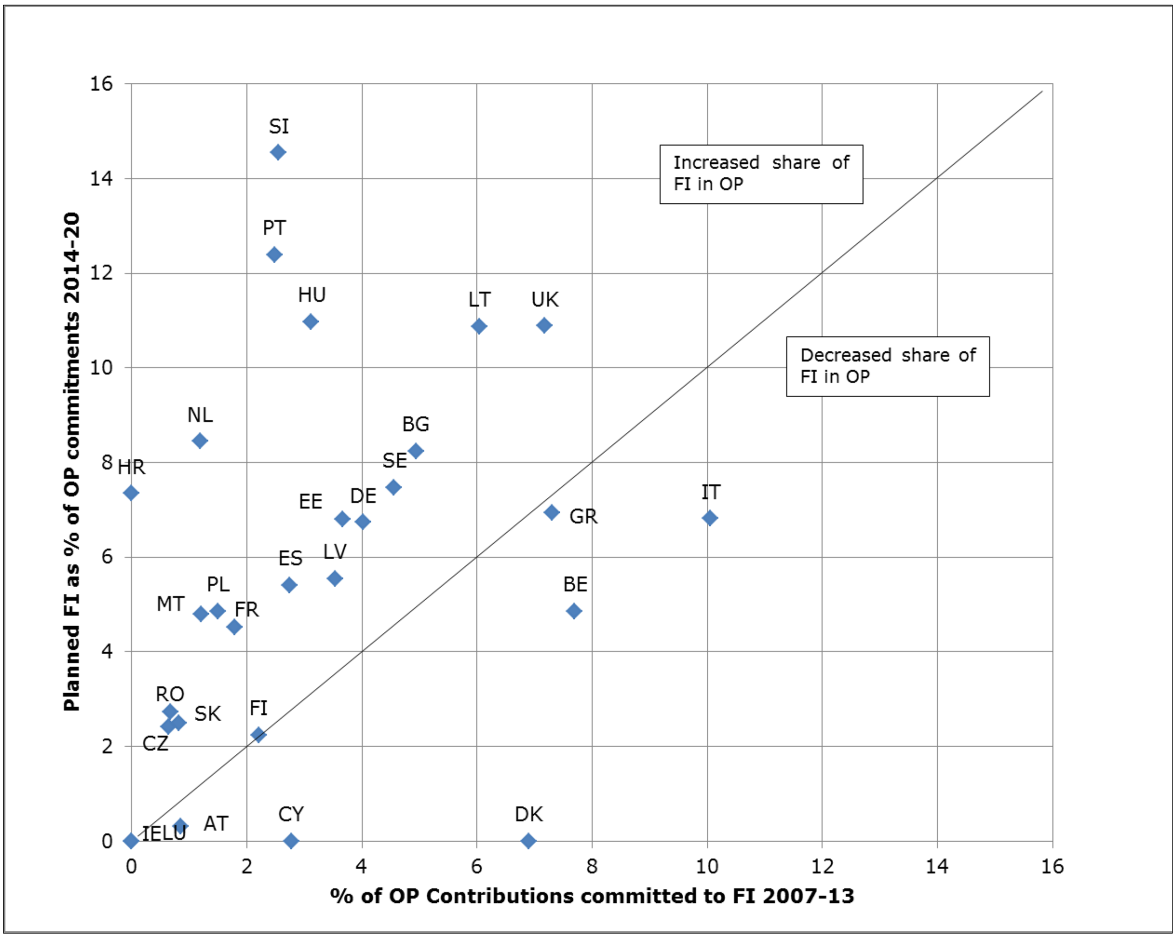
- As before, IE and LU ***do not plan*** to use financial instruments.
- CY and DK may ***cease*** using co-financed financial instruments and AT plans significantly to ***reduce*** their use.
- IT and BE committed the largest shares of OP contributions to financial instruments in 2007-13 (10.1 percent and 7.7 percent, respectively), but ***planned amounts are reduced*** to 6.8 percent and 4.9 percent of OP contributions in 2014-20.
- Five Member States ***plan to commit over 10 percent*** of OP contributions to financial instruments in 2014-20. Some – LT, UK – were already making

[128] See Annex 3 for an overview of the national situation in 2007-13 and 2014-20.

[129] See European Commission (2015) Op cit, Table 2.

significant use of financial instruments in 2007-13 (over 6 percent of OP contributions), but in others – SI, PT, HU – this represents a ***substantial increase*** (from under 4 percent to over 10 percent) in the share of OP resources planned for FIs.

Figure 3.5: Trends in OP commitments to FIs (% of EU OP contributions)



Note: These figures do not include the EFF in 2007-13 or the EMFF in 2014-20.
Source: EPRC calculations.

There are also important shifts in the ***absolute*** amounts of EU funds committed to financial instruments in Operational Programmes. These are shown in Table 3. Clearly the scale of contributions to FIs varies widely between countries and these cannot meaningfully be compared where countries differ significantly in population and/or total OP contributions. However, at country level, Figure 3.6 shows some significant changes in OP planned contributions to financial instruments between funding periods. In particular:

- Seven countries plan to ***reduce*** OP commitments to FI in absolute terms (AT, BE, CY, DK, FI, GR, IT) with significant absolute changes in GR and IT which, as mentioned, committed large shares of OP contributions to FIs in 2007-13.
- Four Member States plan to commit ***more than four times*** the 2007-13 amounts to FIs in 2014-20 (NL, PT, RO, SI).
- A further six plan to ***more than double*** OP commitments compared to the previous period (CZ, FR, HU, MT, PL, SK).
- Many of the remainder were already relatively significant users of FIs in 2007-13 and plan to ***increase their commitments further*** (BG, EE, LT, SE, UK).

Figure 3.6: Trends in OP commitments to FIs (€ and % change), EU amounts

MS	Planned OP contributions to FIs 2014-20	Nominal change in EU amounts 2007-13/2014-20 (€m)	Change in OP contribution to FIs (as % of 2007-13)
AT	3.0	-7.3	-70.8
BE	98.2	-60.6	-38.2
BG	611.9	281.8	85.4
CY	0.0	-17.0	-100.0
CZ	521.0	350.3	205.2
DE	1231.5	206.8	20.2
DK	0.0	-35.2	-100.0
EE	240.3	115.6	92.7
ES	1510.6	556.9	58.4
FI	29.7	-5.6	-15.8
FR	665.8	425.3	176.9
GR	1058.2	-418.9	-28.4
HR	621.8	621.8	~
HU	2365.0	1586.7	203.9
IE	0.0	0.0	0.0
IT	2160.8	-648.5	-23.1
LT	729.4	320.2	78.3
LU	0.0	0.0	0.0
LV	245.1	84.7	52.9
MT	34.0	23.8	233.3
NL	85.7	65.9	334.1
PL	3736.8	2728.4	270.6
PT	2643.7	2112.5	397.7
RO	618.1	489.1	379.2
SE	131.8	57.6	77.7
SI	438.0	333.0	317.2
SK	342.9	248.1	261.7
UK	1194.1	483.7	68.1
EU28	21317.2	9899.3	86.7

Notes: (i) These figures do not include the EFF in 2007-13 or the EMFF in 2014-20; (ii) this table only includes EU amounts and makes no adjustment for price changes.

Source: EPRC calculations.

3.2. What are the main characteristics in the use of FIs at the level of Member States?

For many Member States, the use of co-financed FIs is not decided at national level, and as the FI landscape varies greatly within countries, the picture at the level of the Member State may simply be an aggregation of what is happening under very different OPs. [130] The view at Member State level may therefore obscure, rather than clarify, what is happening within the various OPs. That said, some broad characteristics can be identified:

- There is more continuity than change in terms of how FIs are being implemented in some countries (e.g. DE, PL and UK (Wales), while accommodating modest to high increases in allocations to FIs. Sometimes continuity in existing FI implementation is accompanied by new initiatives – for example, in Sweden there is continuity of the eight regional venture capital FIs under the regional OPs, but accompanied by an FI allocation under a national OP, which will include a national Fund of Funds to support

[130] See Annex 3 for an overview of the national situation in 2007-13 and 2014-20.

equity FIs (Swedish Venture Initiative with EIF) and a national green fund to promote the transition to low-carbon economy.
- Some countries have made a strategic choice to centralise FIs within fewer OPs e.g. in Greece, in 2014-20 only the Competitiveness OP plans to use FIs (whereas in 2007-13, FIs were used in 3 OPs). In Hungary, almost all FIs are now concentrated in the Economic Development OP.
- Change to how OPs are structured within countries has had an impact-on FI implementation, again concentrating FI use. In Estonia, for example, three OPs used FIs in 2007-13; these have been replaced by a single national OP in which FI use has been doubled. In Lithuania also, where two out of four OPs used FIs in 2007-13, these have been replaced by a single national OP, with a significant increase planned in FIs. In Slovenia, one OP now covers ERDF, ESF and CF (replacing three OPs), with more than four-fold increase in planned FI allocations.
- Six Member States are planning to implement the SME Initiative (BG, ES, MT, FI, IT, RO). This required the introduction of a new dedicated OP for that purpose with the whole OP allocation in the form of financial instruments. The relationship to FIs in other OPs has not always been clearly articulated.

Under many Operational Programmes, ***the design and implementation of financial instruments remains in a state of flux*** and the final outcomes are likely to differ from OP plans for FIs in significant respects. In part, this is due to differences in how Managing Authorities have dealt with the obligation to 'set down a marker' for FIs in the OP: some provided an indicative amount, others recorded 'zero' against FIs as form of finance or left the entry blank, though the narrative of the OP left the possibility of using FIs in future open.

Changes in plans for FIs are also affected by the outcomes of the ex ante assessments, which may increase or decrease financial allocations or alter their thematic profile. DG Regio's FI Unit survey in 2015 identified some significant changes in planned FIs even at that comparatively early stage. Indeed, for five OPs where no budget had been allocated in the OP, Managing Authorities reported significant planned spend on FIs:

- CZ: OP Environment (€241.4m)
- IT: NOP Employment (€27.1m)
- IT: NOP Youth Unemployment (€26.0m)
- SK: OP Integrated Infrastructure (€119.0m)
- SK: OP Quality of Environment (€94.1m).

In the case of Czech Republic and Slovakia, these new FI plans represent a significant increase in plans to use FIs (47 percent and 38 percent increases, respectively), and there are notable increases in Greece (26 percent) and to a lesser extent Italy (13 percent). However, some significant decreases in planned spend are also recorded (Croatia, Latvia, Finland) – see Figure 3.7.

Figure 3.7: Initial changes in planned OP allocations to FIs

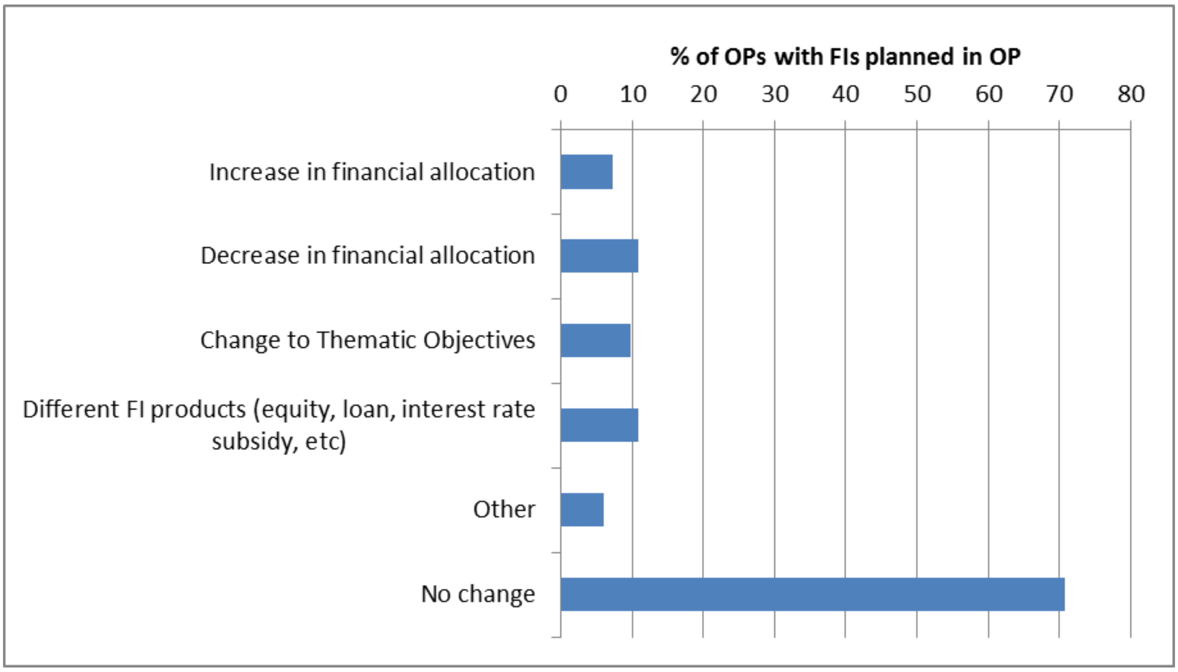
	€m change	% change compared to OPs
CZ	242	46.54
DE	-98	-7.99
EE	-25	-10.30
FI	-8	-27.63
GR	276	26.04
HR	-182	-29.24
IT	271	12.55
LV	-60	-24.34
PL	-218	-5.83
SK	129	37.60
EU28	344	1.61

Note: Only changes of more than five percentage points are recorded here.
Source: EPRC calculations.

These data should be treated with caution since many Managing Authorities reported that, as the ex antes were not complete, the figures being reported in the interim were those indicated in the OP, so for most countries little change was evident at that particular stage.

There is further evidence of the fluidity of FI plans in the response to the Managing Authority survey. Of the 82 respondents with OPs where FIs were planned, 24 (almost 35 percent) said that their plans for FIs had changed in one or more ways (see Figure 3.8). Responses included both the intention to increase and to decrease planned allocations to FIs, plans to change the TOs under which FIs were used, and plans to change the form of finance to use different FI products from those originally envisaged in the OP.

Figure 3.8: Have plans for FIs changed since OP adoption



Source: EPRC managing authority survey.

The reasons for change vary. Managing authorities cite the results of the ex ante assessments, which recommended different financial allocations or decisions not to proceed with FIs under a particular theme. Changes in allocations to FIs have also been attributed to:

- concern that market conditions are not currently conducive to implementation of co-financed FIs (low interest rates, and domestic finance with better conditions available);
- a shift in local domestic priorities requiring a shift in funding allocations within the OP;
- decisions to use recycled resources to fund the planned FI;
- analysis finding that repayable assistance would be more appropriate for the planned intervention;
- a decision to concentrate on fewer instruments;
- a change in the demarcation of the coverage of different OPs; and
- advice from financial intermediaries that planned allocations to an FI were too high.

With some Managing Authorities planning to update or revise ex ante assessments, further change can be expected. At the same, it remains challenging to capture just how plans are changing until the final details of operational FIs emerge.

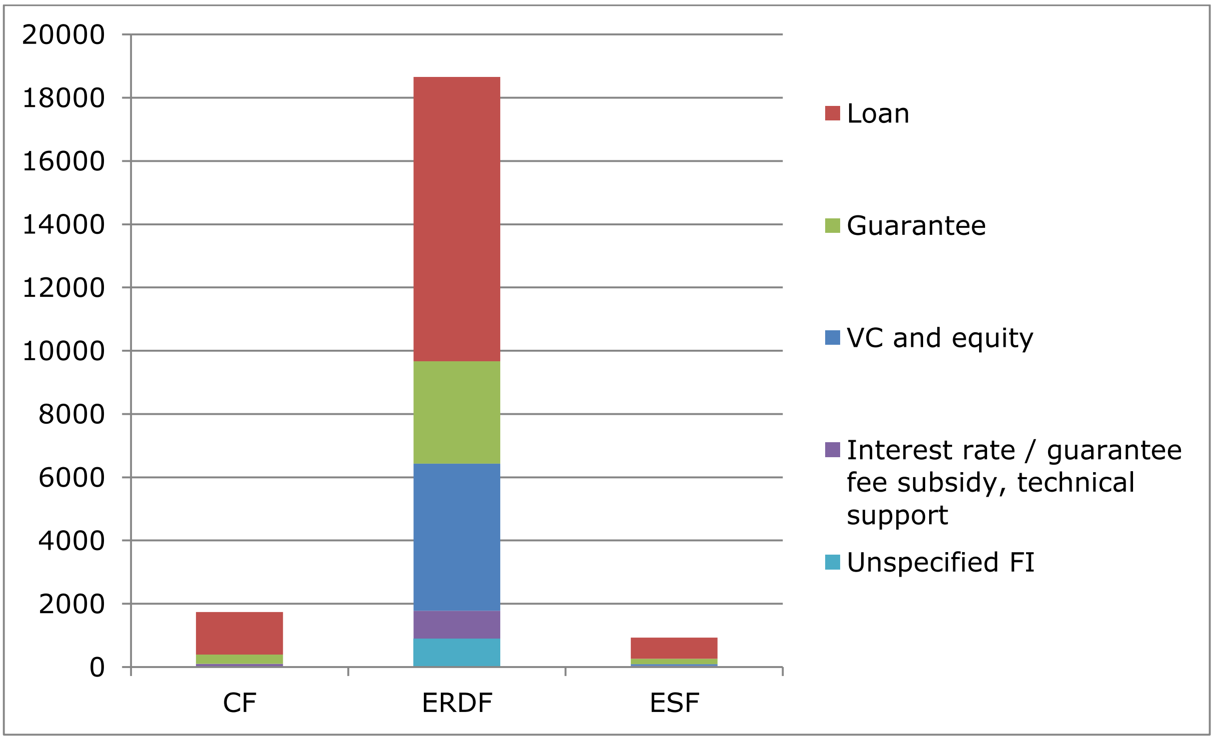
3.3. Which funds do Managing Authorities plan to use for financial instruments? ERDF, ESF and CF OPs

In 2007-13, the use of financial instruments was mainly the preserve of the European Regional Development Fund. All Member States that used FIs used the ERDF to co-finance them, with seven also using the European Social Fund. Six Member States used the European Fisheries Fund for financial instruments. The Cohesion Fund could not be used for financial instruments in 2007-13.

In 2014-20, extension of the policy objectives for which FIs can be used potentially increases the scope for their use under funds other than the ERDF.[131] However, as Figure 3.9shows, ***planned allocations remain predominantly under the ERDF*** and mainly in the form of loans.

[131] The EMFF is dealt with separately (see 3.9) since EMFF managing authorities were not required to record planned expenditure by form of finance.

Figure 3.9: OP indicative allocations to FIs by fund - €m (EU resources)



Note: 'FI not specified' refers to funds under the SME initiative where the precise form is not yet determined.
Source: EPRC calculations from OP data collated by the European Commission.

That said, the overall increase in the planned use of EU resources for FIs under the ERDF and the ESF is broadly the same (approaching double). However, there are differences between Member States – see Figure 3.10. In particular:

- Some countries ***plan to use the ESF for FIs*** where they did not do so in 2007-13 – namely Bulgaria, Greece, Spain, Hungary, Portugal, Romania and Slovakia.
- Some may ***cease to use ESF for FIs*** – namely Estonia and Latvia.
- Seven (of the 15 qualifying) countries ***plan to use the Cohesion Fund*** for financial instruments, with significant sums allocated in Poland and Portugal.

Figure 3.10: Commitments and planned contributions by fund and country

	ERDF 2007-13	ERDF 2014-20	ESF 2007-13	ESF 2014-20	CF 2014-20
AT	10.3	3.0			
BE	158.8	98.2			
BG	330.1	485.2		25.0	101.7
CY	17.0				
CZ	170.7	521.0			
DE	838.2	1149.0	126.1	82.5	
DK	13.3		9.9		
EE	118.7	240.3	6.0		
GR	1308.1	1048.2		10.0	
ES	950.1	1485.6		25.0	
FI	35.3	29.7			
FR	230.3	665.8			
HR		511.8		110.0	
HU	762.1	2310.8		25.6	28.6
IT	2525.9	1992.0	261.3	168.8	
LT	394.7	645.4	14.5	40.5	43.4
LV	147.5	223.9	12.8		21.2
MT	10.2	34.0			
NL	18.5	85.7			
PL	973.1	2582.6	31.1	107.1	1047.1
PT	375.6	2068.5		139.2	436.0
RO	129.0	486.3		131.8	
SE	72.0	131.8			
SI	105.0	382.0			56.0
SK	94.8	278.3		64.5	
UK	662.3	1194.1			
Total	9890.3	18653.2	461.7	930.1	1733.9

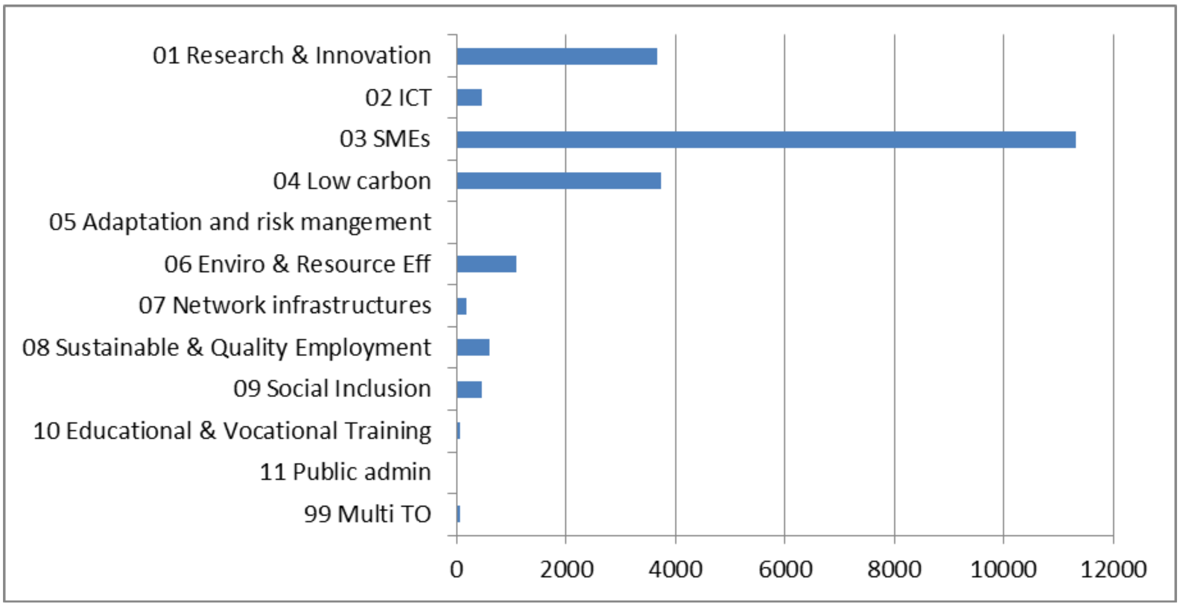
Note: Figures for 2007-13 refer to contributions paid to funds or holding funds while figures for 2014-20 refer to planned OP contributions.
Source: OP data and European Commission (2015) Summary of data on the progress made in the financing and implementing financial engineering instruments.

3.4. Which Thematic Objectives and Investment Areas are being addressed through FIs?

Information on ***FIs by Thematic Objective*** is required in the Operational Programmes. This information has been partially updated by the Commission survey of Managing Authorities enabling, for the most part, the disaggregation FI spending plans under Multi TO investment priorities. This is important as it provides a clearer picture of where FIs are planned – in some Member States FIs were planned under Multi TO priorities that were aimed at SMEs (TO3) and R&D&I (TO1). In others the focus was on urban development with priorities involving low carbon economy (TO4) and environment and resource efficiency (TO6), and sometimes social inclusion (TO9) and/or SMEs (TO3) as well.

Analysis of spending plans for FIs shows that ***more than half of planned FI spend (52 percent) is targeted at SMEs (TO3).*** A further ***17 percent each is aimed at research and innovation (TO1) and low carbon (TO4).*** This means that around 87 percent of all FI spend is planned for these three objectives. Comparisons with 2007-13 are not entirely straightforward because investment is not targeted in the same way, but in general terms there is a diversification of planned spend, though SME support, not surprisingly, remains dominant, as Figure 3.11 shows.

Figure 3.11: OP indicative allocations to FI by TO - €m (excluding EMFF)

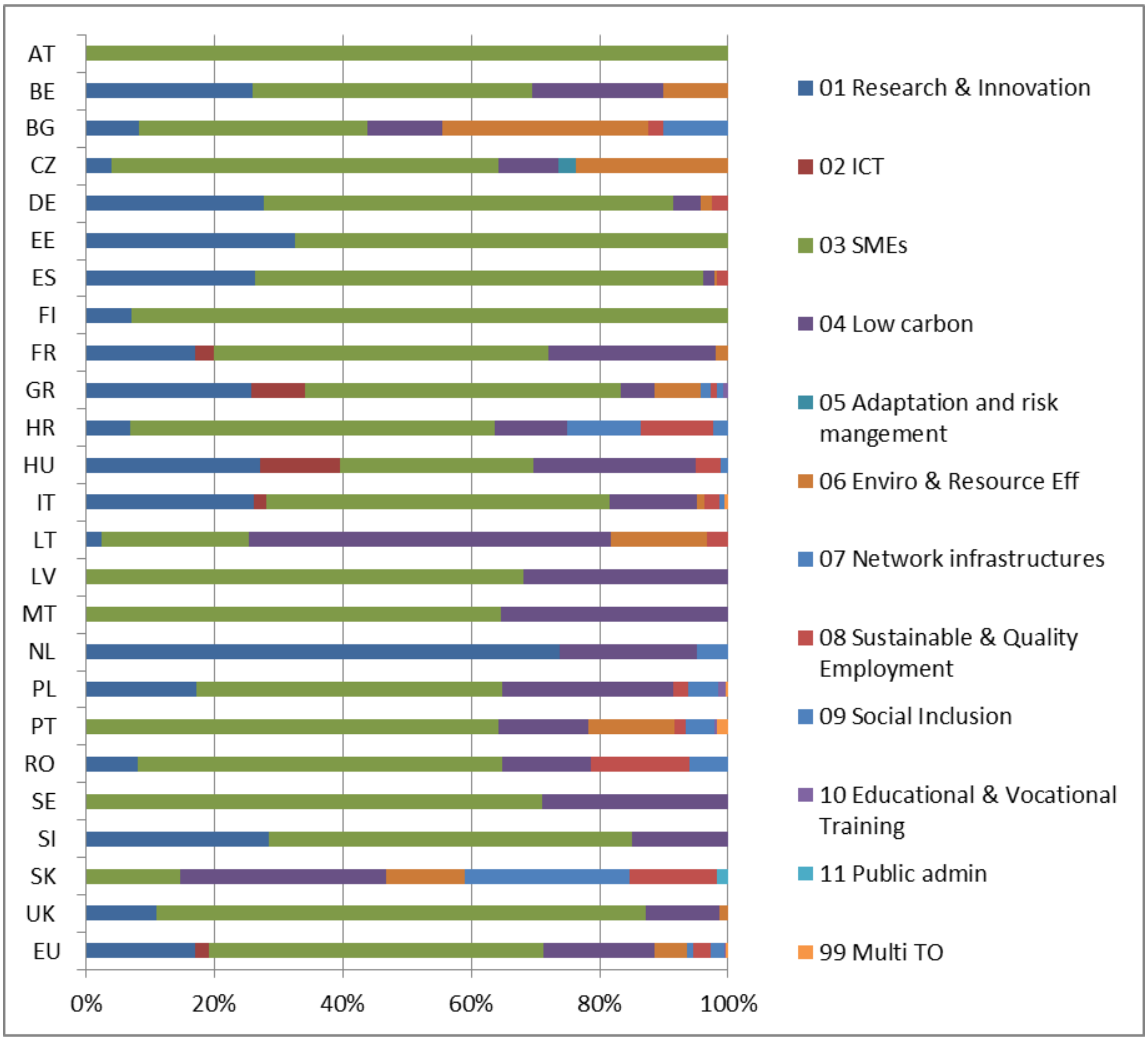


Source: EPRC calculations from data collated by the European Commission. Multi TO refers to Priority Axes that address more than one Thematic Objective.

However, within these aggregates planned spend varies widely between countries, as illustrated in Figure 3.12:

- ***in some Member States, planned spend on FIs for SMEs as a share of total FI spend far exceeds the 52 percent average*** – this is the case in Austria, where FIs are only used under TO3, Finland (93 percent), Sweden (71 percent), United Kingdom (76 percent) and Spain (70 percent);
- similarly, ***planned spend on R&D&I FIs as a percentage of the total significantly exceeds the 17 percent average in some countries*** – for example, in the Netherlands 74 percent of FI spend is directed at TO1, Germany (29 percent), Estonia (33 percent) and Slovenia (29 percent);
- the same is true of ***low carbon economy*** – for instance in Lithuania, 57 percent of FI spend is targeted at TO4, and high shares are also recorded for Malta (36 percent) and Latvia (32 percent);
- ***countries vary in the number of TOs addressed through FIs***. In many Member States with larger ESI fund allocations (though not all), FIs are planned across six thematic objectives or more – as in Bulgaria, Greece, Croatia, Hungary, Italy, Poland, Portugal and Slovakia, whereas elsewhere the focus is much narrower – on just two TOs in Estonia, Finland, Latvia, Malta and Sweden.

Figure 3.12: OP indicative allocations to FI by TO - %, by Member State (excluding EMFF)



Source: EPRC calculations from data collated by the European Commission.

Turning to ***Investment Areas***, the Investment Plan for Europe[132] proposed that Member States should:

> "commit to increase significantly their use of innovative financial instruments in key investment areas such as SME-support, energy efficiency, Information and Communication Technology, transport and R&D support. This would achieve at least an overall doubling in the use of financial instruments under the European Structural and Investment Funds for the programming period from 2014 to 2020."[133]

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[132] Communication from the Commission to the European Parliament, the Council, the European Central Bank, the European Economic and Social Committee, the Committee of the Regions and the European Investment Bank: An Investment Plan for Europe**:** http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM:2014:903:FIN

[133] Member States were recommended to deliver through FIs a percentage of the allocations made in their Partnership Agreements to each of "the key investment areas" as follows: 50% in the field of SME support; 20% in the field of energy efficiency/renewables (CO2 reduction) measures; 10% in the field of Information and Communication Technology; 10% in the field of sustainable transport; 5% in the field of support for Research Development and Innovation; and 5% in the field of environmental and resource efficiency. The use of micro-finance facilities to provide

The Investment Plan was followed up by a letter to Member States from the four ESIF DGs in February 2015.

As mentioned above, information on the planned form of finance and Thematic Objective is required in the Operational Programmes, but data are not explicitly disaggregated by Investment Area. However, as Figure 3.13 shows, there is a 'read across' between the six Investment Areas and the Thematic Objectives (though not vice versa).

Figure 3.13: Thematic objectives (CPR) and Investment Areas

Thematic Objectives for ESIF (CPR)		Investment areas for FIs (Investment Plan for Europe) and suggested proportion spent
1. Research and Innovation	→	RD&I (5%)
2. ICT	→	ICT (10%)
3. SME competitiveness	→	SME support (50%)
4. Low Carbon Economy	→	Measures related to energy efficiency/renewables (20%)
5. Adaptation and Risk Management		
6. Environment and Resource Efficiency	→	Environmental and resource efficiency (5%)
7. Sustainable transport and network bottlenecks	→	Sustainable transport (10%)
8. Employment and Labour Mobility		
9. Social Inclusion and Poverty		
10. Education		
11. Institutional Capacity		

On the basis of this 'read across', initial indications are that, overall, ***apart from R&D&I, planned spend on FIs falls somewhat short of early ambitions*** for FI spend by Investment Area. That said, again there are significant differences between Member States, as illustrated in Figure 3.14:

- Reflecting the aggregate figure, ***many countries exceed the proposed target for R&D&I*** – notably Bulgaria, Estonia, Greece, Hungary, Italy, the Netherlands and Slovenia.
- Only ***Greece and Hungary exceed the proposed target for ICT*** and many do not propose to use FIs for this Investment Area at all.
- Only the ***Czech Republic meets the target for SME support***, but Estonia, Greece, Romania and Slovenia come close.
- ***Six countries meet the target for energy efficiency/renewables*** (Hungary, Lithuania, Malta, Portugal, Sweden and Slovenia), but a significant number do not use FIs to this end.
- ***Five countries meet the target for environmental and resource efficiency*** (Bulgaria, Czech Republic, Lithuania, Portugal and the United Kingdom), but again many do not plan FIs for this purpose.
- ***No Member States meet the target for sustainable transport*** and only three plan FIs for this Investment Area.

preferential loans was also deemed to be helpful to promote self-employment, entrepreneurship and develop micro-enterprises.

Figure 3.14: Planned shares of OP resources for FIs by Investment Area

	R&D&I	ICT	SME support	Energy efficiency/ renewables	Environ. & resource efficiency	Sust. transport
AT	0.0	0.0	1.8	0.0	0.0	0.0
BE	9.8	0.0	17.9	10.4	5.9	0.0
BG	10.3	0.0	36.6	7.3	11.4	0.0
CY	0.0	0.0	0.0	0.0	0.0	0.0
CZ	1.2	0.0	51.7	3.2	9.0	0.0
DE	8.5	0.0	31.5	2.1	3.0	0.0
DK	0.0	0.0	0.0	0.0	0.0	0.0
EE	10.9	0.0	48.3	0.0	0.0	0.0
ES	8.4	0.0	39.5	0.7	0.3	0.0
FI	0.5	0.0	7.7	0.0	0.0	0.0
FR	7.2	2.1	26.3	10.0	1.3	0.0
GR	36.7	14.2	49.0	4.0	3.5	0.8
HR	4.5	0.0	25.8	9.4	0.0	3.8
HU	29.9	42.4	34.4	24.4	0.0	0.0
IE	0.0	0.0	0.0	0.0	0.0	0.0
IT	18.1	2.7	38.0	9.8	1.1	0.0
LT	2.6	0.0	31.3	42.3	14.8	0.0
LU	0.0	0.0	0.0	0.0	0.0	0.0
LV	0.0	0.0	42.7	12.3	0.0	0.0
MT	0.0	0.0	38.2	26.0	0.0	0.0
NL	19.0	0.0	0.0	15.0	0.0	0.0
PL	7.2	0.0	25.4	9.8	0.0	0.0
PT	0.1	0.0	37.8	23.3	19.1	0.0
RO	5.1	0.0	47.1	2.5	0.0	0.0
SE	0.0	0.0	32.2	22.8	0.0	0.0
SI	27.7	0.0	48.3	23.8	0.0	0.0
SK	0.0	0.0	17.0	14.1	3.7	3.4
UK	8.9	0.0	45.0	9.6	9.8	0.0
EU28	**8.9**	**3.5**	**34.0**	**9.5**	**3.1**	**0.3**
Target	***5.0***	***10.0***	***50.0***	***20.0***	***5.0***	***10.0***
Total FI €m	**3667.7**	**468.4**	**11319.7**	**3748.5**	**1089.0**	**189.9**
Total OP €m	**41104.0**	**13308.1**	**33276.3**	**39661.4**	**34993.5**	**58523.8**

Source: EPRC calculations.

Overall, the rationale for using financial instruments in these areas is consistent with the discussion in Section 2.3. However, variations in usage suggest that it is more difficult to address some policy issues through FIs than others. In the areas of innovation and SME support, where FIs are used most, they can be seen to be addressing market imperfections related to informational asymmetries and risk aversion. However, there appears to be more difficulty in addressing externalities relating to information and communication technologies and environmental and energy efficiency issues, perhaps partly owing to the requirement for supported projects to be revenue-generating. The focus of this section is on the rationales *for* using FI; the rationale for *not* using FIs is discussed later (see Section 4.7).

Box 3.1: Financial instruments for ICT

In 2014-20, only OPs in France, Greece, Hungary and Italy have made allocations for FIs under TO2 (Enhancing access to, and use and quality of information and communication technologies (ICT)). Among these, the allocation made in Hungary is by far the most significant, representing 42.4 percent of resources available for ICT under the Economic Development and Innovation OP.

The launch of FIs under TO2 in Hungary has been a response to the problems faced by companies investing in the ITC sector when they attempt to raise finance from banks. In addition to the problems faced by SMEs more generally in accessing funding, the assets available to this sector (e.g. software, broadband network cable) are not accepted by banks as collateral. Returns are only seen over the very long term (average 10-12 years). The ex-ante assessment highlighted some general constraints to broadband development, including the administrative burden (e.g. permits), taxes, and limited technical planning capacity, and proposed a flexible approach combining grant assistance with FIs, as well as a pre-seed/seed capital fund to assist companies at the early stage of their operation. FIs will be used to support the expansion of new-generation broadband networks, projects that improve the competitiveness of the ITC sector internationally as well as ITC upgrading of SMEs. Support is being delivered under a fund of funds: four specific sub-funds are planned – three combined grant and loan FIs and an equity scheme.

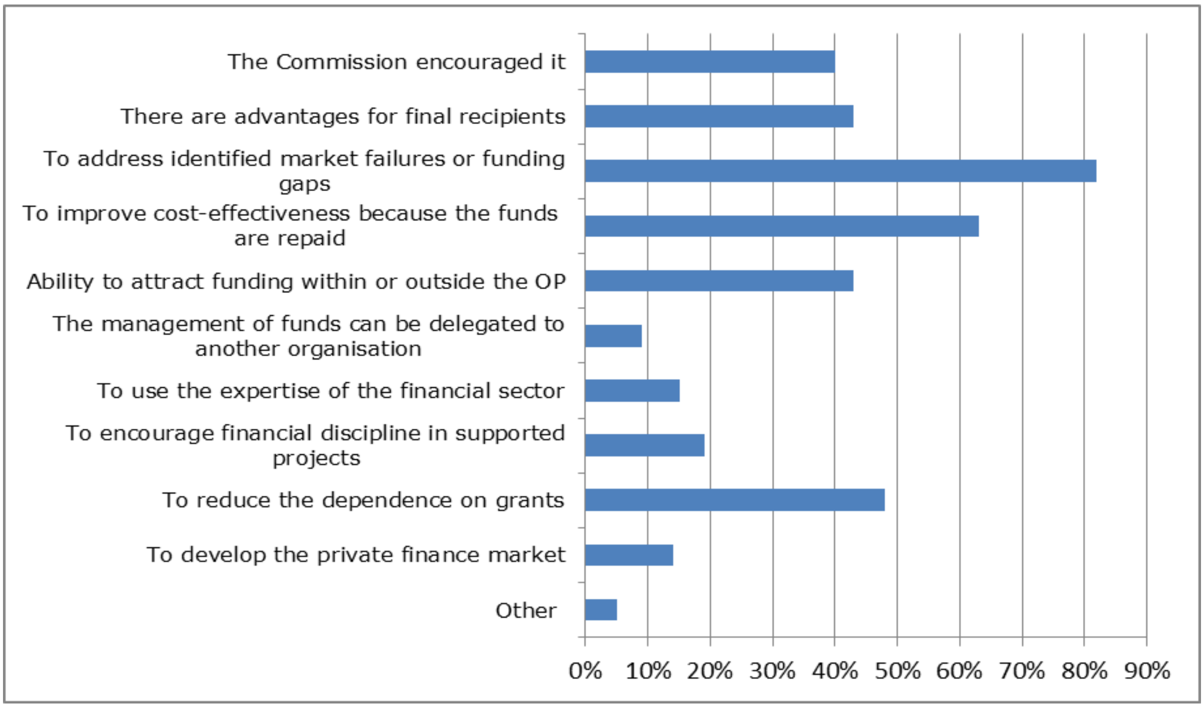
Several recommendations have so far emerged relating to FIs under TO2 from the Hungarian Economic Development and Innovation OP:

- Setting up the FIs has taken longer than expected.
- Administrative capacity required to operate FIs under TO2 is found to be unique; ICT specialists must be involved at various stages of implementation (e.g. call for proposals, project appraisal) so the fund of the funds has engaged external experts.
- As the direction of ICT development is quite unpredictable, financing terms and calls should remain relatively broadly defined.
- There is a need for support for companies to prepare for the receipt of seed/start-up capital (e.g. mentoring and incubation).
- The need for marketing of the FI products among entrepreneurs is evident.
- Lack of direct experience with TO2-related FIs may have contributed to over-ambitious targets having been set.
- The use of combined grant and loan schemes increases complexity, as it involves two funding regimes and two calls (the MA manages the grant element). Two delivery regimes must be harmonised and two sets of procedures must be harmonised.

Source: EPRC Case study research – see Annex 1.

The survey asked Managing Authorities to select up to five factors which were important in the decision to use financial instruments for a given TO (see Figure 3.15). This shows that more than 80 percent of Managing Authorities considered that FIs were needed to address a finance gap or an identified market failure (it is perhaps surprising that not all MAs selected this factor). The next most important factors were to improve cost-effectiveness of spend and to reduce the dependence on grants.

Figure 3.15: Please select up to five factors for using FIs…(all TOs)



Source: EPRC survey of Managing Authorities.

Interestingly, these rationales differ somewhat by Thematic Objective, though some caution must be exercised given the comparatively small sample – see Figure 3.16.

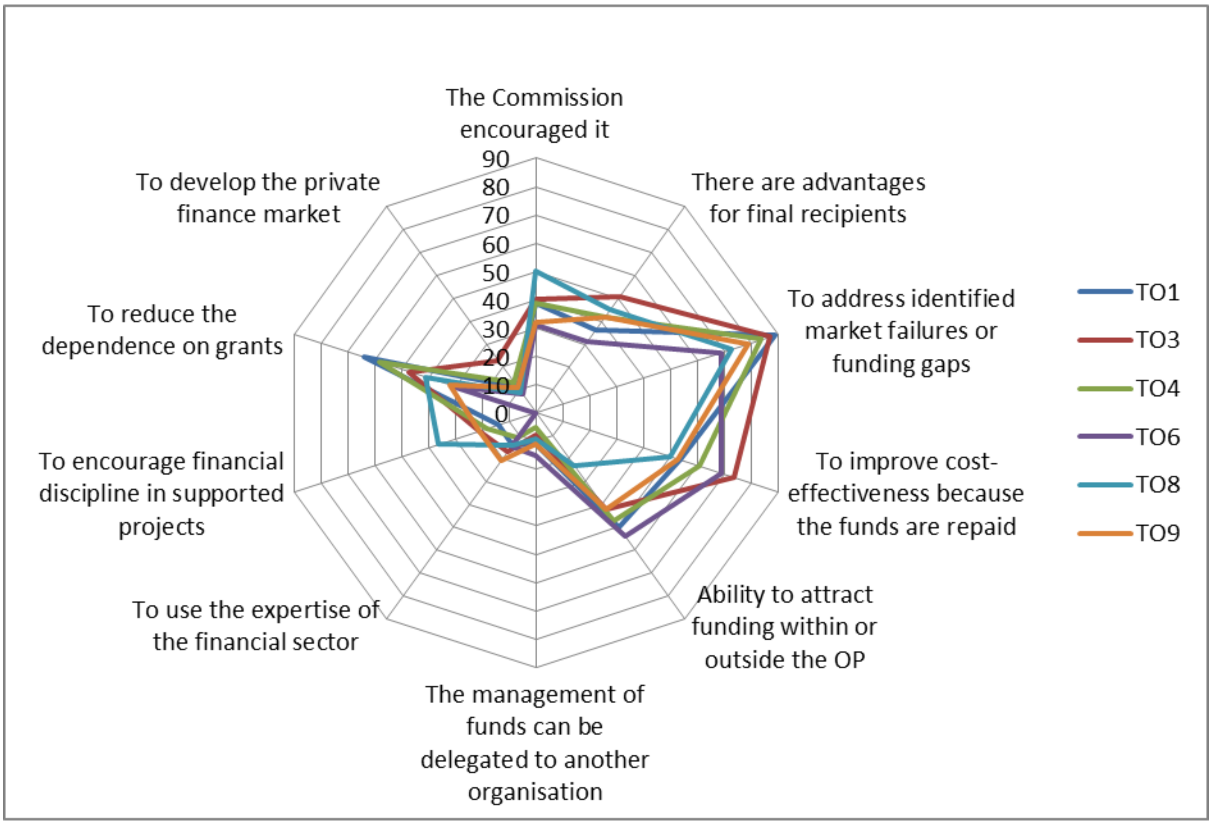
***For all TOs, the need to address finance gaps / market failures was viewed as the most important factor*, but the emphasis varies between TOs.** For TO1 (R&D&I), 89 percent of respondents considered this one of the five most important factors, while for TO6 (environment and resource efficiency), just 69 percent considered this important.

For TO1 (R&D&I) and TO4 (low carbon), the second and third most cited rationales were reducing dependence on grants and improving costs effectiveness.

For TO3 (SMEs), the second factor was also cost-effectiveness, but the third factor was the view that FIs have advantages for final recipients. The ex post evaluation of financial instruments under Cohesion policy 2007-13 suggests that this might relate to issues such as the capacity to cover a larger proportion of investment requirements and/or greater flexibility in spending.

TO8 (Employment and labour mobility) displays a slightly different profile from other TOs. Encouragement from the European Commission is more important for the use of FIs in this TO than any other, and it is the only TO where 'encouraging financial discipline' is a significant factor underpinning the use of FIs.

Figure 3.16: Please select up to five factors for using FIs…(selected TOs)



Note: Only TOs where more than ten Managing Authorities proposed to use FIs are included.
Source: EPRC survey of Managing Authorities.

3.5. What are the key patterns in the planned use of FI at OP level?

Aggregate information conceals an ***extremely varied picture of planned financial instruments at OP level.*** This is partly due to the varying structures of OPs (some national, some regional, some thematic, some covering more than one fund) and their varying size (partly a result of different OP structures, but also a consequence of country size and eligibility for ESI funds).

Setting aside EMFF OPs, which are discussed separately (see 3.10 below), and Interreg programmes[134], where no OP made plans for financial instruments, there are 315 OPs in total. Of these, ***160 OPs allocate funds for financial instruments***. However, the scale of planned financial instruments varies extremely widely both in absolute terms and in their importance within the relevant OP.

Of the 315 ERDF, CF and ESF OPs, ***14 OPs have planned FI spend exceeding €400m***;[135] collectively these 14 OPs alone account for ***over 55 percent of planned FI spend***. As Table 6 shows, however, it does not follow that where planned FIs are large in absolute terms they also account for a large share of OP spend. For example, the Polish OP Infrastructure and Environment allocates over €1 billion to FIs, but this represents less than four percent of OP spend. At the opposite end of the spectrum, some 50 OPs plan to allocate around €20m or less to financial instruments (but this may account for a large share of spend in OPs with small budgets).

[134] Interreg is used as the 'brand name' for European Territorial Cooperation programmes.
[135] EU amount.

An important point to note here is that, under some OPs, the amounts now planned for FIs changed following the adoption of the OPs. In some cases these changes were significant. For example:

- As noted above, OP Environment (CZ) ***now plans €241.4m on FIs which was not envisaged in the OP,*** representing over 9 percent of planned OP spend (which would place this OP in Figure 3.17)
- OP Competitiveness, Entrepreneurship and Innovation (GR) has ***increased the planned allocation to FIs by almost one third*** to €1334 million.
- OP Infrastructure and Environment (PL) now plans FI spend at ***around half the planned amount on FIs*** (cut from €1047 million to €556 million)
- Several OPs now anticipate reduced levels of spend on FI – Latvia (down from €245 million to €185 million); Croatia (down from €512 million to €380 million); Lombardia (down from €221 million to €173 million); and Puglia (down from €220 million to €131 million).

Although there are examples of FI spend expected to increase (e.g. Greece), in the main, among OPs where plans have changed, the trend is downwards, and in some cases by quite significant amounts. Another important observation is the progress with implementation among OPs with significant FI planned budgets. As Figure 3.17 shows, the majority of OPs in this ranking do not have operational FIs; this has potentially important implications for the capacity of planned spend on FIs to be absorbed in practice.

Figure 3.17: OPs ranked by planned allocations to FIs (€m)

MS	OP name	FI Total (€m)	FI as % of OP	Change since OP?	New FI total (€m)	FIs opera-tional
HU	Economic Development & Innovation OP	2235.2	28.9	N		Y
GR	Competitiveness, Entrepreneurship & Innovation OP	1058.2	29.0	Y	1334	N
PL	OP Infrastructure & Environment	1047.1	3.8	Y	556	N
PL	OP Smart growth	892.3	10.4	Y	1095	N
UK	ERDF England OP	882.5	24.3	N		N
PT	ROP Norte	866.2	25.6	N		N
ES	SME Initiative ERDF 2014-20 OP	800.1	100.0	N		Y
IT	NOP Enterprises & Competitiveness	798.4	47.6	Y	864	N
LT	OP for ESIF 2014-2020	729.4	10.9	N		Y
PT	ROP Centro	582.0	27.0	N		N
HR	Competitiveness & Cohesion OP	511.8	7.4	Y	380	N
SI	OP Implementation of Cohesion Policy 2014-20	438.0	14.5	Y	449	N
PT	Sustainability & Resource Efficiency OP	436.0	19.4	N		N
CZ	Enterprise & Innovation for Competitiveness	433.1	10.0	N		N
RO	Regional Operational Programme	336.3	5.0	N		N
PT	ROP Alentejo	269.4	24.9	N		N
ES	Smart growth ERDF 2014-20 OP	252.7	6.4	N		N
LV	Growth & Employment	245.1	5.5	Y	185	N
EE	OP Cohesion Policy Funding 2014-2020	240.3	6.8	N		Y
IT	ROP Lombardia ERDF	221.2	45.6	Y	173	Y
IT	ROP Puglia ERDF ESF	220.0	6.2	Y	131	N
PL	ROP Kujawsko-Pomorskie 2014-2020	204.9	10.8	Y	234	N
DE	OP Berlin ERDF 2014-2020	200.5	31.6	N		Y
BG	OP Innovations & Competitiveness	199.8	18.5	N		N
		14100.5				

Note: The stock of operational FIs is a ‘snapshot’ (spring 2016) and is evolving.
Source: EPRC calculations.

Financial instruments also vary in relative importance within OPs – see Figure 3.18. Six Member States are implementing the SME Initiative, or planning to (BG, ES, MT, FI, IT, RO), so that the whole OP allocation is in the form of financial instruments. Beyond these specific cases, however, ***27 OPs plan to allocate more than 20 percent or more of OP funds to financial instruments***, making FIs a potentially significant component of the overall programme.

In some cases, planned OP contributions to FI are significant in both absolute and relative terms – note that 10 OPs feature in both rankings (marked in bold in Figure 3.18) and together ***account for well over a third of planned OP contributions*** to financial instruments.

Again, as noted above, progress with implementation has been rather modest, with the risk that some programmes may struggle to invest the sums planned for FI in the required timeframe, with implications for absorption under the OP as a whole, given the relative importance of FI within them.

Figure 3.18: OPs ranked by planned allocations to FIs (as % of OP total)

MS	OP name	FI Total €m	FI as % of OP	Change since OP?	New FI total €m	FIs opera-tional
ES	**SME Initiative ERDF 2014-20 OP**	**800.1**	**100.0**	**N**		**Y**
BG	Operational Programme under the SME Initiative	102.0	100.0	N		N
IT	National operational programme SME Initiative	100.0	100.0	N		N
RO	Operational Programme 'SME Initiative' Romania	100.0	100.0	N		N
FI	SME Initiative ERDF 2014-20 OP	20.0	100.0	N		N
MT	Stimulate private sector investment for economic growth	15.0	100.0	N		N
IT	**NOP Enterprises & Competitiveness**	**798.4**	**47.6**	**Y**	**864**	**N**
SE	National ERDF OP for investments in growth and jobs 2014-2020	61.9	46.5	N		N
IT	**ROP Lombardia ERDF**	**221.2**	**45.6**	**Y**	**173**	**Y**
NL	OP West Netherlands ERDF 2014-2020	62.9	33.1	N		N
DE	**OP Berlin ERDF 2014-2020**	**200.5**	**31.6**	**N**		**Y**
FI	Entrepreneurship and skills, Åland Structural Fund OP 2014-2020	1.5	30.2	N		N
ES	Madrid ERDF 2014-20 OP	75.0	30.0	N		N
UK	United Kingdom - ERDF Northern Ireland	91.1	29.6	N		Y
GR	**Competitiveness, Entrepreneurship & Innovation OP**	**1058.2**	**29.0**	**Y**	**1334**	**N**
HU	**Economic Development & Innovation OP**	**2235.2**	**28.9**	**N**		**Y**
PT	**Regional OP Centro**	**582.0**	**27.0**	**N**		**N**
PT	**Regional OP Norte**	**866.2**	**25.6**	**N**		**N**
PT	**Regional OP Alentejo**	**269.4**	**24.9**	**N**		**N**
UK	**United Kingdom - ERDF England**	**882.5**	**24.3**	**N**		**N**
SE	Stockholm	8.0	21.6	Y	9.5	N
IT	ROP Toscana ERDF	85.2	21.5	Y	59.1	Y
DE	OP Bremen ERDF 2014-2020	21.4	20.8	Y	23.1	N
ES	Castilla y León ERDF 2014-20 OP	64.7	20.6	N		N
IT	ROP Marche ERDF	34.2	20.3	N		N
SE	South Sweden	12.2	20.0	Y	11.9	N
NL	OP South Netherlands ERDF 2014-2020	22.7	20.0	N		N

Note: The stock of operational FIs is a 'snapshot' (spring 2016) and is evolving.
Source: EPRC research.

3.6. What is the progress with FI implementation in 2014-20?

The Common Provisions Regulation alters the terms on which financial instruments can be used in ESI funds (compared to 2007-13) since it requires Managing Authorities both to indicate their intention to use FIs in the OPs and to conduct an ex ante assessment prior to introducing them. All Member States at least leave open the possibility of using financial instruments, though the extent to which this is being actively pursued varies.

There are four Member States where ***no OPs currently have planned contributions to FIs.*** In *Ireland* and *Luxembourg*, while the option of using FIs is mentioned, there is no evidence of any intent to pursue this and neither country used FIs in 2007-13.[136] In Cyprus, reference is made to the possibility of using FIs for a number of priorities, to be defined on the basis of an ex ante assessment. However, if the ex ante is undertaken and co-financed FIs introduced, it seems probable that this it would be part of the Cyprus Entrepreneurship Fund, through which a number of financial products are provided with EIB involvement. In Denmark, a 'gap analysis' was conducted in 2015 and this noted the opportunity for co-financed FIs to address market gaps, but political consensus to pursue this, while also ensuring additionality to the national Danish Growth Fund, has not yet been reached. Both Cyprus and Denmark used co-financed FIs in 2007-13.

The remaining ***24 Member States plan to use FIs***, at least in some of their Operational Programmes. The nature and scale of FI plans varies considerably between and within Member States. It is worth noting that in most countries, there is no real *national* perspective on co-financed FIs – uptake and implementation varies markedly across OPs within countries, especially regional OPs.

Progress in implementation also varies markedly within and between countries. Many Member States are still at quite an early stage in FI implementation (although the picture is continually changing and developing). For example, Croatia, which has reduced initial allocations planned for FIs, does not yet have any FIs at operational stage; Belgium, Bulgaria, Czech Republic, Finland, Latvia, Netherlands, Poland, Slovenia and Romania all appear to be at similarly early stages. In Greece, a comprehensive update of the ex ante assessments is being procured.

Progress is mixed in France, where almost all regional OPs foresee using FIs, but only two are so far operational. In England (UK), the consolidation of what was formerly ten regional ERDF OPs in 2007-13 into one national ERDF OP, alongside the move to a localism approach,[137] has complicated the potential use of FIs. Overall, 31 Local Enterprise Partnerships or Intermediate Bodies are interested in running FIs under TO3, these are likely to be grouped into five large funds (of a minimum of £25m ERDF) and four smaller stand-alone funds (ranging from £1m to over £3m ERDF each). Eleven LEPs are interested in the urban development or energy efficiency (JESSICA 'type') FIs, and four are interested in the Managing Authority's Local Impact Fund FI model.

However, there are examples of faster progress among both very large and relatively small FIs. In Hungary, where FIs are concentrated in the Economic Development OP, and represent an important component of that OP (29 percent), progress has been hindered by difficulties with the selection process, but nevertheless a funding agreement has been signed for a major loan scheme (€1399m) and this has now been launched. In Austria, where only one (relatively small) regional FI has been launched (€3m), implementation has progressed quickly and awards have already reached final recipients.

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[136] Note that examples of lapsed and non-users of FIs are explored as a case study in Annex 1 to this study.

[137] Reflecting the role of the Local Enterprise Partnerships.

Figure 3.19 provides a broad indication of the intended uptake of and progress with the implementation of FIs at the level of ERDF, CF and ESF OPs. It is important to stress that the number of OPs in each case does *not* equate to the number of ex ante assessments, funding agreements or financial instruments related to them – there is no direct relationship between these.[138] Nevertheless, it is evident that progress in implementing FIs has been rather modest.

Figure 3.19: Progress with implementation of FI (by number of OPs)

	OPs (excl EMFF)	OPs planning FIs (excl EMFF)	OPs with 'ex antes' complete	OPs with signed funding agreements	OPs with FIs in set-up	OPs with FIs operating
AT	2	1	1	1		1
BE	7	2	0			
BG	8	5	5	1	1	
CY	2	0				
CZ	8	3	3			
DE	32	19	15	9	2	8
DK	2	0				
EE	1	1	1	1	1	1
ES	45	13	6	1	5	1
FI	3	3	2			
FR	40	26	10	1		2
GR	18	1	1			
HR	2	2	2			
HU	7	4	0	1		1
IE	3	0				
IT	51	24	8	7		6
LT	1	1	1	1	1	1
LU	2	0				
LV	1	1	1		1	
MT	3	2	1	1		1
NL	5	2	0			
PL	22	19	19			
PT	12	11	11	8	10	
RO	7	4	2		1	
SE	11	9	9			
SI	1	1	1			
SK	7	4	3			
UK	12	5	4	5	4	1
ETC	76	0				
TOTAL	391	163	106	37	26	23

Notes: Data as at spring 2016. EMFF OPs are dealt with separately as they were not required to provide a breakdown by form of finance; figures for Spain, Poland and Germany each include an OP where financial instruments are provided for in the OP, but no budget is indicated. The number of OPs where some funds are at least notionally allocated to FIs is, therefore, 160. It is important to stress that this table is merely as snapshot of an evolving situation.
Source: EPRC research.

[138] For example: one ex ante assessment may cover FIs in more than one OP; there may be more than one ex ante assessment within one OP; and there may be more than one funding agreement within an OP and/or multiple financial instruments within an OP.

Setting aside Interreg OPs, none of which planned FIs, of the remaining 315 ERDF, ESF and CF OPs, over half plan to offer at least some support in the form of financial instruments.[139]

A significant number of ***ex ante assessments*** have been completed – an estimated 143 at the time of writing, though not all have been published.[140] Information on ex ante assessments is not easy to obtain; their existence may not be known until publication, and patterns of publication appear patchy.[141] As discussed in Section 3.7, a variety of approaches have been adopted to ex ante assessments, with some Managing Authorities undertaking ex ante assessments in blocks or stages, and other undertaking updates of existing studies. In addition, ex antes assessments may have been undertaken at Fund level (e.g. for ERDF) either within one OP or across several, for all funds within an OP, for specific instruments or financial products already envisaged or for specific Thematic Objectives. Consequently it is not straightforward to quantify progress and to assess the extent to which FIs planned in the OPs have been the subject of an ex ante assessment. Nevertheless, it is evident that if FI plans under some OPs are to be taken forward, a considerable number of ex ante assessments remain to be done.

Information on ***funding agreements*** is limited, partly reflecting the sometimes commercially sensitive nature of contractual arrangements. In addition, more than one funding agreement may be required to implement a financial product within an OP, so the number of OPs with funding agreements provides only a partial view of the status of planned FIs within OPs.

Last, results from the desk research and the online survey of Managing Authorities show that at least 22 OPs have ***operational financial instruments***. Most of these are in either Germany or Italy, and many appear to be an extension of existing financial products. These are discussed in more detail in Section 3.9.

3.7. How have ex ante assessments of FIs been approached?

The obligation to produce an ex-ante assessment[142] is one of the key novelties for the 2014-20 programming period. While only 143 of the ex antes completed are currently published, from these it is possible to distinguish the variety of different methods used in carrying out the assessments. Figure 3.20 provides a breakdown of the available studies, categorising the various approaches into ex antes, which have been organised at the level of national and regional OPs, for specific FIs, with a thematic focus, or at the level of the ESI Fund.

The ***most common approach taken so far is for ex-ante assessments to be focused on national or regional OPs***, with 65, over 45%, of all ex-antes conducted at the level of the OP. The majority of these are regional ex-antes, reflecting both the significantly greater number of ROPs and the particular approach taken in certain Member States, with France, Poland and the UK conducting almost exclusively regional ex-ante assessment in line with the OPs. This proportion can be expected to increase

[139] Including FI-only SME Initiative OPs adopted in Bulgaria, Finland, Italy, Malta, Romania and Spain.

[140] Copies of the ex ante assessments available to the research team are stored in the Strathcloud FI library – see Figure 1 and Figure 2.

[141] Although ex ante assessments are required to be published within three months of completion, it is not clear what constitutes a complete ex ante.

[142] The completion of the survey demonstrated that there is still some confusion amongst MAs as to the distinction between the ex-ante evaluation of the OP and ex-ante assessment for FIs. As such, the reported numbers of completed ex-antes may be incorrect.

further as many MAs for Italian ROPs have commissioned a number of ex-ante assessments, which are yet to be published.

In total, ***39 ex-antes have been conducted for specific financial instruments*****.** However, this is not reflective of all Member States as 36 of these are from Germany. This focus can be seen as the result of the prior experience of implementing FIs in the 2007-13 period. In Germany many of the ex-antes were for specific regional instruments such as the *ProFIT Darlehen* and *KMUFonds* under the Berlin 2014-20 ERDF OP, which were operational in the previous programming period. The assessment sought to determine the appropriate scale and focus to continue using these FIs. The same is the case in Austria where the only ex-ante commissioned was to continue the *HightechFonds* operated in Upper Austria.

Figure 3.20: Approaches to ex ante assessments

MS	NOP	ROP	FI	Fund/ Multi-Fund	TO / Investment Area	Total ex-antes published
AT			1			**1**
BE		1				**1**
BG	3					**3 (+SMEI)**
CY						**0**
CZ	5				1	**6**
DE	1		36		1	**38**
DK						**0**
EE					2	**2**
ES		**4**				**4 (+SMEI)**
FI	1					**1 (+SMEI)**
FR		16			2	**18**
GR					3	**3**
HR	1					**1**
HU	1				5	**6**
IE						**0**
IT	2	4	1		9	**16 (+SMEI)**
LV					2	**2**
LT					2	**2**
LU	1					**1**
MT						**0 (+SMEI)**
NL			1		3	**4**
PL	1	19				**20**
PT					4	**4**
RO				1		**1 (+SMEI)**
SK				1		**1**
SI				1		**1**
SE				1		**1**
UK		4				**4**
Total	15	50	39	4	34	**142**

Notes: (i) for Greece, Revised versions of the GR ex-antes are expected as current drafts are considered insufficient; (ii) Almost all IT Regional OPs have ex-antes underway; (iii) Only block 1 for England ERDF OP is complete but still included.
Source: EPRC research.

For all available ex-antes, ***34 have approached FI provision thematically or review an individual Investment Area,*** spanning across ESI Funds and national and regional OPs. In Portugal, all four studies carried out are extensive thematic ex-ante assessments, comprising enterprise support, energy efficiency, urban development and innovation and social entrepreneurship. Each ex-ante covers the relevant national thematic OP and the seven ROPs.[143] Similarly, Hungary has produced a series of studies for each Thematic Objective being used for FIs, with ex-ante assessments for Thematic Objectives 1, 2, 3, 4 and 8.

Few ex-antes have been conducted at the level of a single ESI Fund or of multi-funds, with only four published to date. Romania's only published ex-ante covers the ERDF and ESF, across a number of OPs and Thematic Objectives. In Sweden, an ex-ante focuses on all ERDF activities, focusing on one national OP and eight ROPs.

Most published ex-antes have been conducted by private sector consultants. In only a very few cases the MA has carried out the assessments themselves, such as in Italy and the UK (Scotland). It is common that where more than one ex-ante assessment has been conducted in a Member State or region, the same consultant has been contracted to complete many of the other studies.

The ex-ante assessment ***methodology also varies*** between Member States, with some using several differing methods across all ex-antes and others adopting the same approach for each study. In the case of Italy, where separate ex-antes have been conducted using a thematic, instrument and OP-specific focus, it is unclear what the relationship between the findings of each study is. Similarly, for the SME Initiative, a single Union-level ex-ante assessment has been conducted negating the need for Member States to carry out individual studies. However, for the Member States which have opted into the SME Initiative, this leads to a lack of clarity on the status of the findings from other ex-ante assessments conducted prior to opting in (especially those carried out relating to Thematic Objective 3). Again in Italy, a number of regional ex-ante assessments have been conducted recommending the use of FIs under Thematic Objective 3, and there is no indication as to the relationship between the instruments. In other cases such as Bulgaria and Romania, ex-ante assessments and preliminary studies into SME financing make the recommendation to implement the SME Initiative.

Despite the various approaches taken, in all cases ***the ex-ante assessments closely follow the regulatory framework*** as laid out in the Common Provisions Regulation (CPR), taking each of the steps of Article 37 (2)(a)-(g). Where the ex-ante has been conducted after the publication of the ex-ante methodology (April 2014)[144], the studies have cited and used the structure and approach provided. However, while the methodology recommends the assessors conduct the study in two blocks (first, market assessment and second implementation and delivery), almost all ex-ante assessments published have been completed in a single study. There are few exceptions, such as the EIB-led England ERDF OP ex-ante, conducted at the regional level and for which only Block One has been published to date.

3.8. Who are the principal targets of financial instruments?

Many OPs contain information on potential target recipients of FIs. The information provided varies greatly in level of detail – while some OPs provide no information at all, others describe a very detailed range of potential FI recipients for different OP Priority Axes or Investment Areas. The descriptions of target recipients have generally been ***written prior to FI ex ante assessments being carried out***, so including a broad potential target group gives Managing Authorities wider scope for tailoring future FIs according to the recommendations of any ex ante assessment. Many OPs have therefore ***not yet decided or refined their target final recipients*** for FIs.

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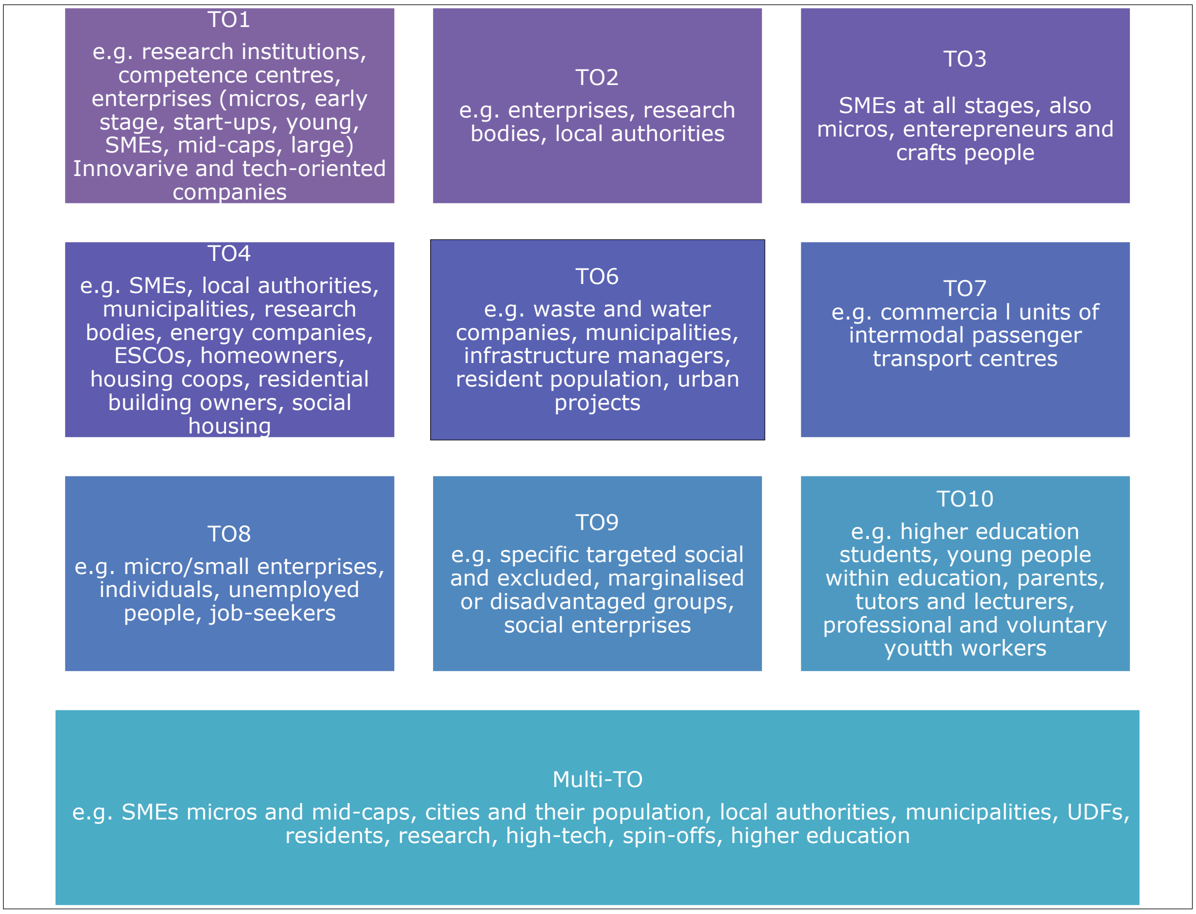
[143] Regional OPs for the North, Centre, Lisbon, Alentejo, Algarve, Azores and Madeira.

[144] Fi-compass (2014) Ex-ante assessment methodology: http://ec.europa.eu/regional_policy/sources/thefunds/fin_inst/pdf/ex_ante_vol1.pdf

According to the OPs, ***enterprises are the principal focus*** of planned FI activity in 2014-20. Support for enterprises can include a broad scope of activity, as well as, in some cases, very specific targets. OPs envisage FIs potentially targeting entrepreneurs, start-ups, micro-businesses, SMEs, mid-caps and large companies. More specific targets, which have been described in OPs, include: geographic targeting (e.g. within the Bratislava region, mountainous areas in Friuli-Venezia-Giulia and mid-caps in the Mezzogiorno); sectors or types of firm (e.g. creative and key technologies, high-tech firms, innovative firms, research-oriented firms, family businesses), and stages of firm development (start-ups, growth-oriented firms). Enterprise support is envisaged mainly under TO 3, but also under TOs 1, 2, 4, 8, 9 and the multi-TO Priority Axes.

OP Priority Axes using FIs also often target local authorities and municipalities. Cities, Urban Development Funds/urban projects, and various housing-related targets also feature (covering a broad range of potential targets – e.g. social housing, owners of residential buildings, collective properties, residents). FIs targeting individuals feature in ESF OPs, for example, targeting unemployed people, job seekers, economically inactive young people, elderly people, disabled people, migrants, addicts, students, community workers, volunteers, and marginalised young people and their parents. There are also examples of FIs potentially targeting water supply and wastewater management companies, energy companies, ITC companies, renewable energy professionals and social enterprises.

Figure 3.21: Potential target final recipients of FIs by TO (as described in the OPs)

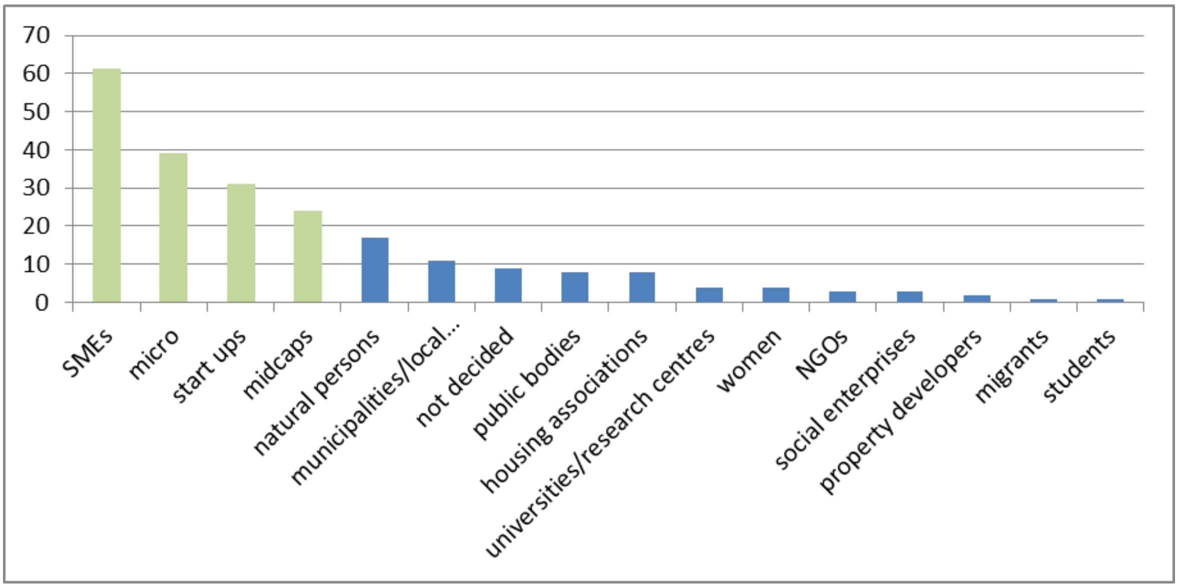


Source: OP data

It is **difficult to assess ex ante whether the target group for FIs is expanding in 2014-20**. The online survey of Managing Authorities **confirms the emphasis on**

enterprise support among the few FIs which have already reached advanced planning or operational stage. However, a wider range of potential recipients is already represented, even if at low levels, suggesting that FIs in 2014-20 may eventually achieve a broader reach.

Figure 3.22: Target final recipients: FIs in operational or advanced planning stage 2014-20 (number of FIs)



Source: EPRC survey of Managing Authorities.

3.9. What is the scale and nature of operational financial instruments?

Information gathering for this study took place in the period February to May 2016. This exercise suggests that at least **23 *OPs had operational or nearly operational FIs***. In this context, 'operational' or 'nearly operational' means that funding agreements have been signed and funds are reaching, or will soon be available to, final recipients. Of the total, 20 are ERDF OPs, and three are ESF OPs. This amounts to over 60 individual FIs, with most OPs having launched multiple FIs, sometimes under different OP Priority Axes.

As might be expected among the 'first wave' of operational FIs, many appear to ***build on previous experience in 2007-13***. The German *Länder* ERDF OPs have been particularly successful in launching their 2014-20 FIs, all of which take the form of specific funds (i.e. not within Fund of Funds structures). Examples are the German *Länder* of Bayern, Berlin, Brandenburg, Mecklenburg-Vorpommern, Niedersachsen, Sachsen, Schleswig-Holstein and Thüringen. In Germany, FIs implemented at *Land* level are in most cases managed by public entities, state banks or limited liability companies with public majority shares. In a few cases private enterprises have been involved in fund management, primarily where equity products are involved.

With a few exceptions, the FIs that are already operational (or nearly so) ***largely address enterprise support (TO3);*** all types of financial product are represented – i.e. loans, guarantees and equity.

There are some examples of operational FIs for ***research and innovation (TO1) and low carbon economy (TO4).*** *Breizh up* is an equity co-investment FI launched under the Brittany ERDF OP (FR) which targets regional SMEs with innovation potential, in support of the region's Smart Specialisation Strategy. In addition, Berlin ERDF OP has launched two venture capital FIs, aimed at undertakings in the creative industry and in key technology fields in the seed-und start-up phase, and the ProFit loan fund for R&D

projects, aimed at SMEs and research facilities. Regarding TO4, several FIs have been launched, for example:

- LfA Energiekredit (EFRE-Projekt 2014B) in Bavaria (DE),
- KMU-Fonds Umwelt in Berlin (DE), and
- the ENEF Fund of Funds (LT), which includes two specific FIs, one offering loans for financing renovation of central government buildings and the other providing guarantees for commercial bank loans for street lighting modernisation projects. The FIs are intended to promote the energy service companies (ESCO) market in Lithuania.

Figure 3.23: Operational and near-operational FIs (as at spring 2016)

MS	OP	Fund	TO	No of FIs	FI name(s)	EU contrib. (€m)
AT	Growth and Employment	ERDF	3	1	• OÖ HightechFonds	3.0
DE	OP Bayern	ERDF	3 4	4	• Bayern Kapital Innovationsfonds EFRE • EFRE-Projekt 2014A • EFRE-Projekt 2014B • EFRE-Projekt 2014C	10.0 7.5. 10.0 7.5
	OP Berlin ERDF	ERDF	1 3 4	5	• KMU-Fonds • ProFit Darlehen • VC Fonds technologie • VC Fonds Kreativwirtschaft II • KMU-Fonds Umwelt	51.7 78.8 30.0 20.0 20.0
	OP Brandenburg	ERDF	3	4	• Frühphasen-und Wachstumsfonds • Brandenburg-Kredit Mezzanine II • Mikrokredit Brandenburg • ProFIT Brandenburg (Darlehensteil)	60.0 22.0 8.0 90.0
	OP Mecklenburg-Vorpommern	ERDF		1	• BMV-Darlehen	N/A
	OP Niedersachsen	ERDF		1	• MikroSTARTer Niedersachsen	N/A
	OP Sachsen	ERDF		3	• Nachrangdarlehensfonds II zur Verbesserung der regionalen Wirtschaftsstruktur • Technologiegründerfonds Sachsen + • Darlehensfonds zur Markteinführung innovativer Produkte Sachsen	N/A
	OP Schleswig-Holstein	ERDF		2	• Beteiligungsfonds für KMU (EFRE IV) • Seed- und Start-up-Fonds II (EFRE V)	N/A
	OP Thüringen	ERDF		4	• 2 equity funds • 2 loan funds	N/A
	OP ESF Federal Germany	ESF		1	• Mikromezzaninfonds Deutschland	N/A
EE	OP for Cohesion Policy Funding	ERDF		3	• ESTFund Fund of Funds - Venture Capital Fund - Expansion Capital Fund - Business Angel Co-Investment Fund	60.0 *(30)* *(15)* *(15)*
ES	SME Initiative	ERDF	3		• SME Initiative	800.0
FR	OP Bretagne	ERDF	3	1	• Breizh up	8.0
	OP Nord-pas-de-Calais	ERDF	4	1	• CAP 3ème Révolution Industrielle	12.5

MS	OP	Fund	TO	No of FIs	FI name(s)	EU contrib. (€m)
HU	Economic Development and Innovation	ERDF	1 2 3 4 8	19	• Fund of Funds Hungarian Development Bank - 19 specific funds	2,235.2
IT	National OP Active Employment Policies	ESF		1	• Revolving Fund SELFIEmployment (Invitalia)	50.0
	National OP Youth Employment	ESF		1	• Revolving Fund SELFIEmployment (Invitalia)	N/A
	ROP Liguria	ERDF	1 3 4		• Loans and guaranteed credit (IP 3c) via Artigiancassa	N/A
	ROP Lombardia	ERDF	1-4		• Open calls: • FRIM FESR 2020 • Line R&D FM Finlombarda (combined) Line 3.b.2.1 and 3.b.2.2 on cultural and tourist attractors (combined)	N/A
	ROP Piemonte	ERDF	1-4		• SME Fund	N/A
	ROP Toscana	ERDF	1 3 4		• Revolving loan fund and guarantee fund, calls are open via Toscana Muove	N/A
LT	OP Structural Funds Investments	ERDF	4	2	• Energy Efficiency Fund (ENEF)	80.0
UK	Northern Ireland	ERDF	3	6	• Co-Investment Fund • Crescent Capital • Kernel Capital • TechStart NI SME • TechStart NI Queens University • TechStart NI University of Ulster	23.7 25.1 25.1 14.6 1.3 1.3

Source: EPRC national expert research; EPRC online survey of managing authorities.

The ENEF Fund of Funds in Lithuania is one of several ***Funds of Funds*** which have been launched. Of these, the Hungarian Development Bank Fund of Funds is the largest, with 19 specific funds within it, and a total EU contribution of €2,235 million. The funding allocated was the maximum available under the relevant Priority Axis of the Economic Development and Innovation OP, which was an FI-only Priority. Due to the tripled allocation of resources compared to 2007-13, the OP applied a broad, open approach, covering TOs 1, 2, 3, 4 and 8.

In addition, FIs ***combining ESIF and EFSI resources*** have been launched in Estonia and Région Les Hauts de France (Nord-Pas-de-Calais/Picardie) (FR):

- EstFund (EE) – launched under the Estonian OP for Cohesion Policy Funds (ERDF, ESF, CF) involves creating a Fund of Funds with a budget of €60 million: €48 million from ERDF (which will be managed by the EIF) and €12 million from the EIF's co-investment, as well as €35.2 million expected from private investors (TO3). The Specific FIs under the FoF will provide equity to final recipients, and include a Venture Capital Fund (€30 million), an Expansion Capital Fund (€15 million), and a Business Angel Co-Investment Fund (€15 million). EstFund will target smaller and earlier stage investments, operating in a complementary way to the existing Baltic Innovation Fund. EstFund operates as a cross-border instrument; ESIF funds will be invested in

Estonian SMEs and some private investor contributions can be invested outside Estonia.

- CAP 3ème Révolution Industrielle (TRI) - The TRI fund launched by Région Les Hauts de France (Nord-pas-de-Calais/Picardie) (FR) will assist business-led investments in 'low carbon economy' projects (TO4). The total budget of up to €37.5 million is made up of €15 million from ERDF (€12.5 million as an FI and €2.5 million as a grant from TA), €5 million from Crédit Agricole Nord de France (commercial bank/private investor), and an EIB loan of up to €20 million, backed by an EFSI guarantee.[145] The TA element will be used to fund technical, environmental or economic studies, either helping project promoters implement their projects or providing independent performance evaluation.

Additional details on a selection of operational FIs are provided in Annex 4.

3.10. What are the plans for and progress of financial instruments under the EMFF?[146]

In the last planning period, use of financial instruments under the European Fisheries Fund (EFF) was limited. Six Member States set up FIs under the EFF in 2007-13, accounting for just 1.5 percent of EFF funding.[147] Half of the FIs set up were guarantee schemes, the other half were loans – see Figure 3.24.

Figure 3.24: European Fisheries Fund FIs in 2007-13

Member State	FI name	Product type	Budget (€ m)
Bulgaria	Guarantees for aquaculture SMEs	guarantees	N/A
Estonia	Loans for aquaculture SMEs	loans	36
Greece	Guarantees for aquaculture, processing and vessel modernisation	guarantees	35
Latvia	Latvian Credit Fund (combined with EAFRD)	loans	7.2
Netherlands	Netherlands Fisheries Investment Fund	loans	3.5
Romania	Guarantees for aquaculture SMEs	guarantees	17.5

Source: Based on data in Scoping study (2015)

The scoping study carried out for *fi-compass* reviewed Partnership Agreements (PA) and *draft* EMFF OPs, and carried out a consultation exercise to assess Member States' intentions for FI use in 2014-20. At that time (May 2015), nearly two-thirds of Member States reported firm or tentative plans to use FIs. However, only three Member States had at that point completed or initiated the relevant ex ante assessments.

Looking to ***2014-20***, the *approved* OPs and the online survey of managing authorities suggest that planned FI use under EMFF has not changed significantly from the 2015 scoping study outcomes:

- Only five Member States outlined definite plans to use FIs in their EMFF OPs.[148]

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[145] https://www.fi-compass.eu/sites/default/files/publications/presentation_20160322_paris_ESIF_Virginie-Dubart_Guillaume-Thome_EN.pdf

[146] Note that the potential use of FIs under EMMF is also explored as a case study – see Annex 1.

[147] Poseidon Aquatic Resource Management Ltd, Eurofish International Organisation, Framian BV and Vivid Economics Ltd (2015) Scoping study for the use of financial instruments under the EMFF and related advisory support activities, Final Report, fi-compass. https://www.fi-compass.eu/sites/default/files/publications/EMFF_SCOPING_STUDY.pdf

[148] Defined as having allocated a budget for FIs in the OP.

- Of these, only three have commissioned ex ante assessments (EE, ES and NL). These have been completed, and those for Spain and Estonia have been published. However, no funding agreements have yet been signed, and no EMFF FIs are operational.
- Among the 'tentative' OPs, one ex ante assessment is in progress (HR).

Figure 3.25: 'Planned' FIs and ex ante assessments under the EMFF

Ex ante status	Tentative FI plans	Definite FI plans (budget assigned)
No ex ante yet	BE, EL, IE, LV, RO, UK	IT, LT
Ex ante underway	HR	
Ex ante completed		EE, ES, NL

Source: EPRC research

Among the five EMFF OPs with definite plans for FIs, ***around €80 million has been earmarked***, with Spain allocating the largest absolute amount, but more significant allocations in Estonia and the Netherlands as a proportion of the EMFF total.

Figure 3.26: Scale and progress of planned EMFF FIs

Member State	Ex ante assessment status	€ million	Proportion of OP (%)
Estonia	Completed	10	9.9
Italy	None	20	3.7
Lithuania	None	2	3.2
Netherlands	Completed	5.5	5.4
Spain	Completed	42.75	3.68
Total		80.25	

Source: EPRC research

In ***Estonia***, the EMFF OP states that FIs are planned for supporting the implementation of productive investments, especially for 'facilitating developmental leaps' and reducing distortions of competition. The rationale provided is to improve the availability of capital for investments and help to ensure sustainable aquaculture development because fishermen and aquaculture firms (which are all self-employed and micro/ small enterprises) continue to experience difficulties in accessing loans that would enable investments to be made prior to receiving EMFF support. Based on the positive experience of using EFF FIs in 2007-13, and considering that commercial banks are not interested in offering loans of less than €100,000, Estonia planned (as of 2015) to use around 8 percent of the EMFF budget for FIs (equity and loans) for SMEs in the Estonian aquaculture and processing sector. An ex ante assessment was published in 2014;[149] it recommended four types of financial product:

- a growth loan for micro and small enterprises,
- a long-term investment loan,
- guarantees, and
- equity investments.

The online survey confirms that the Estonian Managing Authority plans to introduce loans to support productive investment in fishing and aquaculture sectors, and processing and marketing activity by aquaculture enterprises. FIs will address TOs 3 and 8. The following were given as the main rationales for using FIs in both TOs to:

- address identified market failures or funding gaps,
- improve cost-effectiveness because the funds are repaid,

[149] This was commissioned by the Ministry of Rural Affairs and carried out by Ernst & Young Baltic. It covered both the Estonian RDP and EMFF OP.

- attract funding within or outside the OP,
- encourage financial discipline in supported projects, and
- reduce the dependence on grants.

In ***Italy***, where no ex ante assessment has yet been carried out, the EMFF OP foresees the potential use of:
- loans: to enhance the added-value of fishing activity and its quality, foster energy efficiency investments, support productive investments in aquaculture and invest in product processing,
- micro-credit: to promote the diversification of fishing income through investments in complementary activities and support young fishers in making the initial investment to start a business,
- guarantees: to secure loans for investments in innovation, aquaculture and preservation of bio-marine resources, and
- equity: to fund fast-growing businesses in the sector (technological innovation, productive processes).

The rationales given for using FI use in Italy include: the need to facilitate credit access and address the undercapitalisation of fishing and aquaculture businesses; the promotion of FIs by the European Commission; the revolving nature of FIs and their ability to attract leverage; and their less distortive effect in the market (compared to grants).

The EMFF OP for ***Lithuania*** foresees the potential use of FIs in 2014–20 and close links with the implementation of FIs funded under the Rural Development Programme. Indeed, the fund manager of FIs implemented under the two programmes was expected to be the same. The OP indicates that FIs can potentially be used in the implementation of a range of different measures, including:

- the reduction of the impact of fishing on the marine environment,
- improvement of knowledge of maritime conditions,
- protection and regeneration of marine biodiversity, and
- processing of fishery and aquaculture products.

The use of EMFF–funded FIs in Lithuania is expected to lead to faster and more effective implementation of the Common Fisheries Policy and to improved access to finance in the fisheries sector. Soft loans are mentioned in the OP, but types of FIs are expected to be agreed after the completion of the ex ante assessment. A 'free–standing' ex–ante assessment was begun for EMFF co–funded FIs. However, it was discontinued and no conclusions regarding EMFF co–funded FIs were reached. A new ex ante assessment may be commissioned, but no information is available about the timing of any new assessment.

In ***Spain***, the ex ante evaluation of the EMFF OP highlighted the opportunity to make use of FIs in the measures for diversification and new sources of income, added value, quality of products and productive investments in aquaculture. Following this recommendation, FIs will be centralised in CDTI and SEPIDES (two Spanish public companies). The evaluation also highlighted that a combination of FIs with grants would be the most effective form of intervention. Publicity and information about EMFF FIs were identified as key to effectiveness. Therefore, the OP foresees an increase in technical assistance related to FI use. The rationale provided for using EMFF to fund FIs relates to liquidity and access to finance issues faced by Spanish fisheries firms (especially SMEs), due to the ongoing economic crisis, and consequent reduction in the budgets of the Spanish administration and a lack of public finance. FIs are seen as important to improve competitiveness, promote entrepreneurial initiatives and private investment. FIs are also seen as important for the implementation of innovation and technological development projects at national and international level. FI support is foreseen for two types of initiative:

- business innovation projects which support the practical implementation of scientific and technologic know-how in the productive system. These projects are carried out in cooperation with research institutes, technological centres or universities.
- loans at subsidised interest rates for technology investment projects carried out by companies. Eligible initiatives include the incorporation and active adaptation of emerging technologies, creating processes of adaptation of technologies to new markets, industrial design and the implementation of new or significantly improved production methods, including significant changes in techniques and/or ICT applications.

An ex ante assessment for EMFF FIs in Spain was carried out by PwC and published in November 2015. The assessment recommends the set up of three FIs:

- guarantee instrument for finance in the fisheries sector,
- loan instrument for finance in the fisheries sector, and
- loan instrument for technological development and innovation.

In addition to the developments at national level, in the framework of the Spanish autonomous communities, the Department of Rural Matters and Sea in collaboration with the Galician regional development agency (IGAPE) foresees the creation of a regional FI co-financed by the EMFF. During the course of the programming period, new EMFF FIs could be set up at regional level for different aims such as local participatory development.

Future EMFF FIs in the ***Netherlands*** will depend on the outcome of an evaluation of the pilot revolving fund launched in 2014.

For Member States with only ‘tentative’ plans for FIs, there is limited information available on planned FIs. This includes:

- **Belgium:** possible use of guarantees linked to the national FI for fishery and aquaculture (FIVA).
- **Ireland:** potential FIs in the seafood processing and aquaculture sectors.
- **Romania:** addressing difficulties in accessing finance by fishermen, producers and entrepreneurs, an issue that was emphasised during consultations with local fisheries stakeholders, potentially by using guarantees.
- **United Kingdom:** consideration of long term loans to support processing and marketing, productive investments in aquaculture, diversification in fisheries and innovation in all sectors.

In all cases, however, decisions await the findings of any ex ante assessment.

4. Practical, legal and administrative issues in the use of financial instruments co-financed by the ESI funds

Key findings

- Different forms of support suit different project types – MAs view SME development (TO3), low carbon economy (TO4) and research and innovation (TO1) as most appropriate for FIs.
- MAs perceive that the key disadvantage of FIs is their administrative complexity.
- FIs are considered by MAs to be harder to administer than grants due to lack of experience, the quality of the regulatory framework and the associated administrative burden.
- Financial intermediaries can lessen the administrative burden of FIs. Some MAs also consider that for final recipients the administrative burden of FIs is lower than grants.
- Value for money is not intrinsic to the form of support. Sometimes grants can offer better value for money than FIs, because of administration costs.
- FIs are perceived by MAs to have economic impacts on several levels and sometimes for less outlay than grants.
- The choice of financial product by MAs is driven primarily by the outcome of the ex ante assessment.
- Competition or overlaps between forms of finance can be minimised by appropriate programme design.
- Overall the main reasons for not using FIs is their unsuitability for planned projects (e.g. non-revenue-generating); however, under TO3 and TO4, where FIs are most used, the main reason for *not* using FIs is the perceived lack of demand among final recipients.
- Views on Off-the-Shelf FIs are broadly positive, but uptake has been low due to timing of the Regulation and a desire for greater domestic flexibility.
- MA perceptions of the new legislative framework are mixed. A key concern is the uncertainty arising from the scope to interpret the Regulations.
- The obligatory ex ante assessment is viewed very positively.
- MAs would like more, and more effective, direct contact with the Commission for guidance on specific needs.
- Factors that could improve the uptake of FIs include changes to the State aid rules, simplification, improved communication with the Commission, training, information and advice.

The overall objective of this section is to identify the practical, legal and administrative capacity issues which influence the use (or non-use) of co-financed financial instruments. The section draws on the outcome of the online survey and policymaker interviews and is structured around a series of issues and questions that arise from the terms of reference and which are also explored in a series of case studies which are annexed to this report.

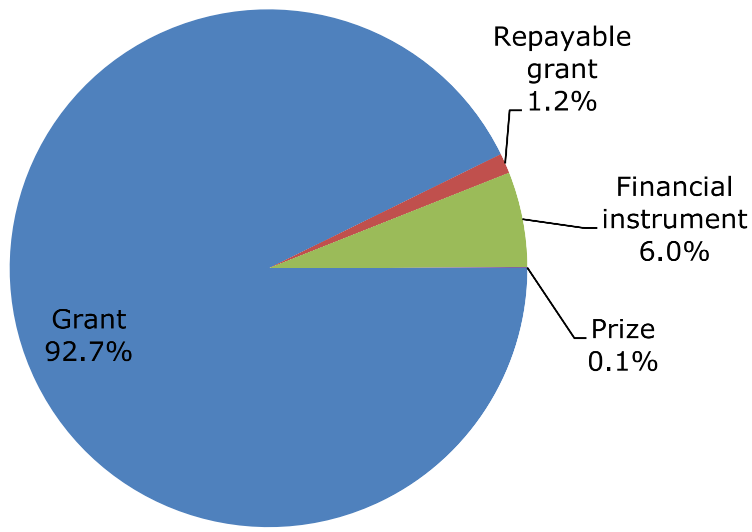
Historically, grants have been the mainstay of support under the Structural and Cohesion Funds, but increasingly the Commission has promoted other forms of support, especially financial instruments, across a wider range of policy areas. The Common Provisions Regulation (CPR) provides that:[150]

> [t]he ESI Funds shall take the form of grants, prizes, repayable assistance and financial instruments, or a combination thereof.

[150] Regulation 1303/2013, Article 66.

In exploring perceptions of different forms of support, it is important to note that the extent to which Member States have experience of the various instruments varies widely: although financial instruments are rising in importance, they account for just six percent of OP commitments in the new period and are used in just 160 OPs (from a total of 412); prizes and repayable grants are used even less.

Figure 4.1: Planned spend by form of support



Source: European Commission.

Reflecting this, in many cases the analysis of the survey responses from Managing Authorities distinguishes between the perceptions of those MAs using, or planning to use, financial instruments in 2014-20, and those with no such plans.

4.1. How and why are different forms of support more appropriate for different objectives?

Policymakers in Managing Authorities identified a number of advantages and disadvantages of the different forms of support. In general, little was known about prizes, and as mentioned these are little used, however views on the different forms of support were not primarily conceived in terms of pros and cons, but rather in terms of the type of project for which they were suitable. That said, the key disadvantage of grants is perceived to be their lack of sustainability and the risk of creating a subsidy culture while the key disadvantage of financial instruments is considered to be their administrative complexity.

Policymakers in MAs identified several project characteristics which they considered made ***grants the most appropriate choice*** to support a particular project*:*

- Activities with small or no profits for the recipient, but which have wider benefits, such as positive environmental effects.
- Projects with particularly long cost recovery times.
- High risk projects – particularly the early part of the innovation cycle (fundamental research and proof of concept).
- Projects which require an incentive effect or which aim to change the behaviour of recipients – i.e. they are in the wider interest, but would not be undertaken in the absence of a grant.

- Construction of public infrastructure (research centres, universities) where the recipients are public bodies and the infrastructure will remain public.
- Areas of public policy interest like social exclusion or social development that are not commercially oriented.
- Special sectors - energy, environment and water management, some public services or projects are not commercially viable but for some reason important (projects that do not generate enough financial flows).

Some respondents also noted that grants could be more appropriate in the current low interest rate climate:

> "In the current market environment with large amounts of liquidity in the system and low interest rates, some FIs could be considered as redundant, as they do not offer much value added for final beneficiaries. In these cases, FIs could be substituted by grants." (Managing Authority interview)

Others note the suitability of different instruments in relation to the domestic context:

> "Financial instruments may be too advanced for our market. From the analysis carried out, we need to intervene in what is usually theoretically referred to as the 'death valley' period… if [firms] cannot pass this stage they will surely disappear and grants could help in this respect." (Managing Authority interview)

While a few considered that grants were the only suitable instruments:

> "All activities under ETC programmes are better suited to grants. Cooperation is opposite to what you can call 'bankable'… you cannot set up a cooperation project with a loan." (Managing Authority interview)

> "Grants are more appropriate for both public and private activities. The volume of subsidy is much higher, they bring immediate liquidity without increasing the level of debt, and they help improve the rating through the increased own capital and thus to decrease the interest rate burden. In particular for public activities, FIs are pointless as the public bodies are either first class debtors or cannot take on any more loans" (Managing Authority interview)

Respondents also noted that (typically) grants are more attractive to recipients and better understood by applicants, though these features do not, of themselves, make grants more appropriate.

Several characteristics of FIs make them potentially attractive as an option for using in ESIF programmes, particularly the revolving nature of funds, access to a wider range of financial tools for policy delivery, private sector involvement and expertise, and the potential to attract private sector support (and funding) for public policy objectives.[151] In terms of specific projects supported by ESIF programmes, ***financial instruments are considered most suitable*** for activities that are likely to make a financial return, or generate savings for the recipients, but also for activities which have the scope to attract additional resources from the private sector or sources such as the EIB.

> "FIs are particularly interesting for start-ups and technology spin-offs… working with other VC providers is promising… other kinds of grants would not reach this scene" (Managing Authority interview)

[151] European Commission (2014) Financial instruments in ESIF programmes 2014-2020. A short reference guide for managing authorities.

In this regard, the activities or targets most consistently cited as suitable for FIs are SME development (TO3), supporting the shift to a low carbon economy (TO4) and, to a lesser extent, research and innovation (TO1). In part, this is because MAs already have some experience of using FIs in these areas. Also, MAs consider that suitable projects with the necessary features (ability to generate a return or savings, ability to attract additional resources) are most likely to be found under these TOs. These areas are where funding gaps have been most clearly identified. There is also a clear 'fit' with national and regional priorities. At the same time, the wider investment climate is considered to have an impact on the suitability of FIs:

> "FIs for TO4 are being modified at present and the current FIs do not work. Low interest rate loans for CO2 measures are not an incentive on account of the generally low interest rates" (Managing Authority interview).

Some considered that support for entrepreneurs under TO9 (social inclusion) could be a suitable target for FIs, but others considered that grants (or a combination of grants and microfinance) would be more appropriate. Similarly, there were mixed views on support for vocational training, with some Managing Authorities taking the view that this could generate suitable returns, and other considering that it would take too long or be unlikely to do so.

Some Managing Authorities also note that the suitability of FIs for certain types of *projects* (as opposed to Thematic Objectives or Investment Areas) ***depends on the administrative capacity of the Member State*** to implement such instruments and deal with the audit requirements; others noted concerns at being able to absorb funds in the form of FIs because of the complexity of the instruments concerned.

Perspectives on ***repayable grants are more mixed***. Many Managing Authorities have no view, having had no experience, but some were dissuaded from using repayable grants owing to the administrative conditions, or because they had no experience of using them.

> "Repayable assistance is not indicated in the OP and is not used, however, it was considered. Main factors against using it were conditions linked to implementation of repayable assistance – implementation must follow rules for grants, not rules for FIs which imply more important administrative burden." (Managing Authority interview).

Others consider that repayable grants could be useful in specific circumstances – this case for low carbon:

> "Repayable grants are now being considered for TO4 as a way to convince potential beneficiaries to invest in energy efficiency - if there is no return on investment/energy savings, they do not have to repay the grant" (Managing Authority interview).

Some take the view that repayable grants have some of the advantages of FIs:

> "Repayable grants would be applied for SME and in the area of cohesion. Managing authority is proposing the use of FI firstly, and in case, when FI are not appropriate because of the lack of financial feasibility of the projects, the use of repayable grants is foreseen. The administrative burden is high and administration system of repayable grants is quite complicated as in case of grants but this form of support is marked with the advantages of FI related to efficiency of investments and possibility to finance more projects." (Managing Authority interview).

However, others are less convinced and suggest that there is little point in using repayable grants if FIs are used. Some are more critical:

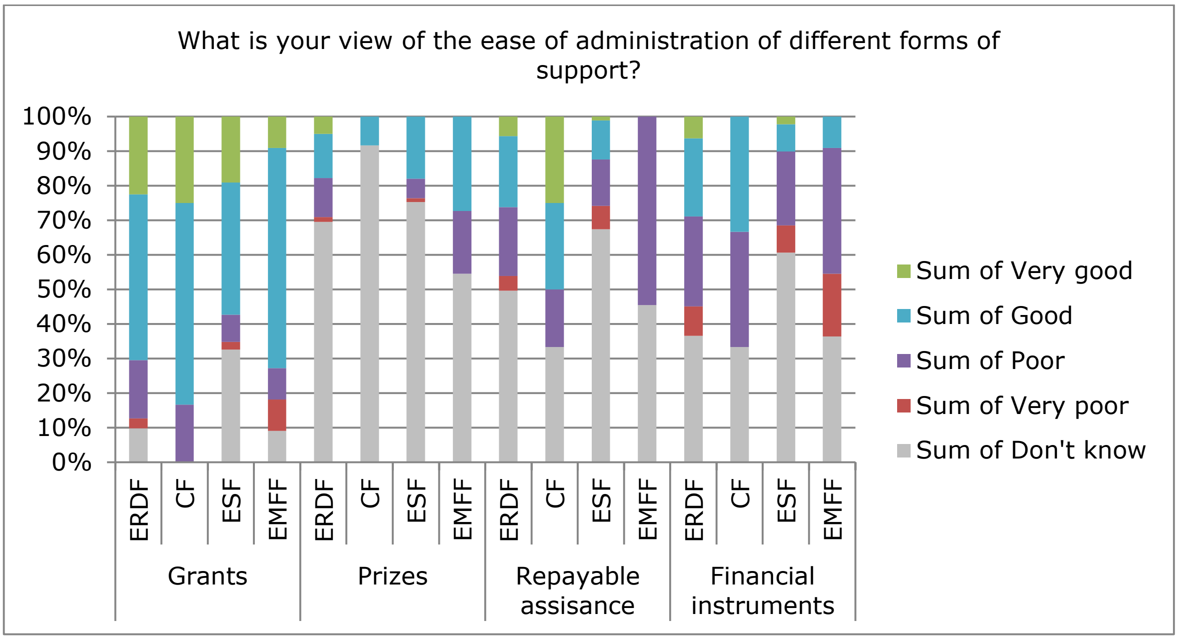
"More of a gimmick than anything – didn't seem to deliver any greater benefit than a typical grant". (Managing Authority interview).

"Repayable grants have no pros; cons are they are ambiguous, complex, open to misuse… (the deliberate setting of) targets/triggers/milestones for payback which will never be achieved." (Financial intermediary)

4.2. Ease of administration: how do different forms of support compare?

An important issue that emerges from the discussion on the relative merits of different forms on intervention is how easy or otherwise they are to administer. Figure 4.2 summarises the perceptions of Managing Authorities by Fund and by form of support.

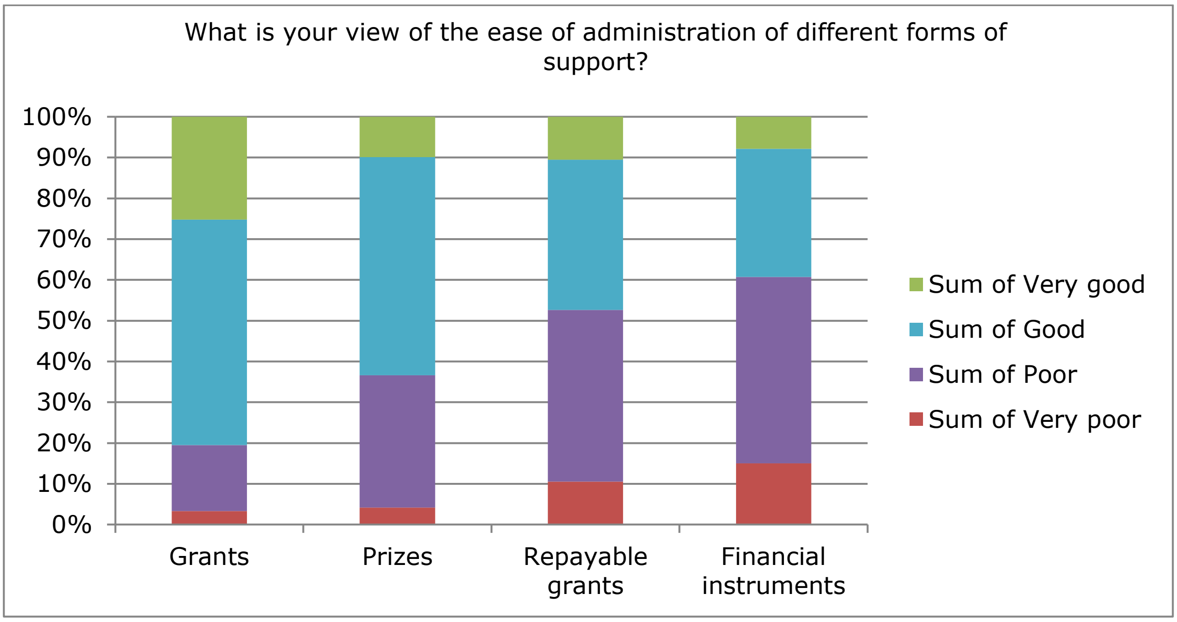
Figure 4.2: 'Ease of administration' (all respondents, by Fund)



Source: EPRC online survey of Managing Authorities.

Lack of familiarity with some instruments is reflected in the high proportion of 'don't knows', except in the case of grants. However, a clearer picture emerges when those without an opinion are excluded.

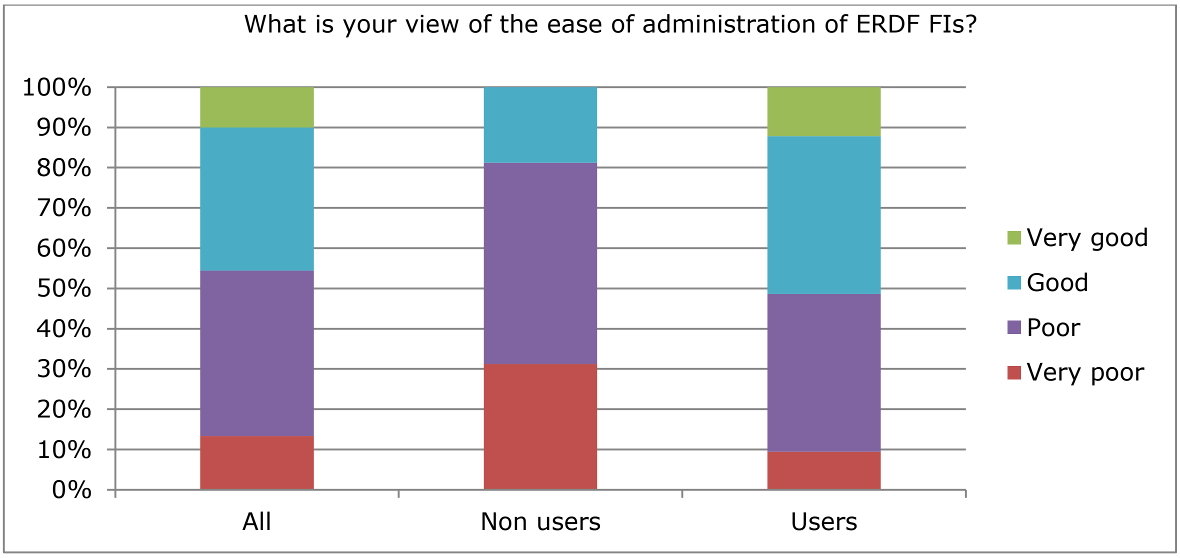
Figure 4.3: 'Ease of administration' (all Funds, excluding 'D/Ks')



Source: EPRC online survey of Managing Authorities.

On this basis, Figure 4.3 shows that over 80 percent of Managing Authorities considered 'ease of administration' of grants to be good or very good; by contrast, over 60 percent of Managing Authorities thought 'ease of administration' of financial instruments to be poor or very poor. Experience with a given form of support is an important dimension to perceptions of ease of administration. As Figure 4.4 shows, FI users are markedly more positive about ease of administration of financial instruments than are non-users of FI: over 80 percent of non-users perceived FI ease of administration to be poor or very poor[152] compared with fewer than 50 percent among FI users.

Figure 4.4: 'Ease of administration' (ERDF MAs, excluding 'D/Ks')

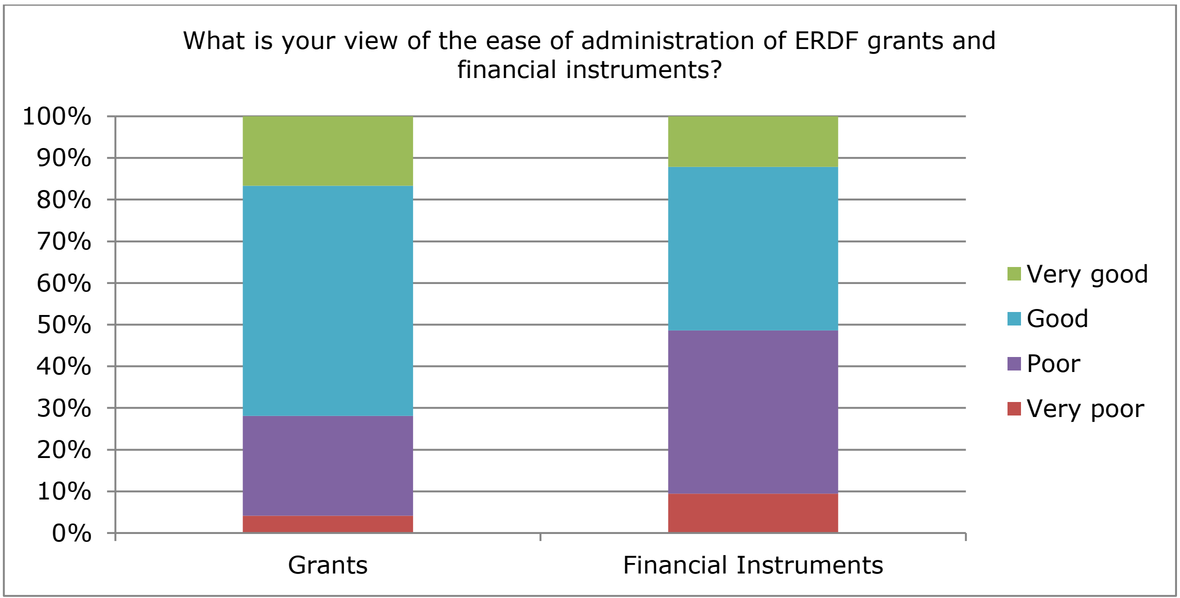


Source: EPRC online survey of Managing Authorities.

[152] Around two-thirds of non-users of financial instruments answered 'don't know' to perceptions of the 'ease of administration' of FIs.

Also interesting, is how Managing Authorities which use financial instruments consider them in comparison with grants. Figure 4.5 shows that **MAs with experience of both types of support consider FIs to be significantly harder to administer than grants**.

Figure 4.5: 'Ease of administration' (ERDF MAs using FIs, excluding 'D/Ks')



Source: EPRC online survey of Managing Authorities.

While the online survey results provide some quantification of perceptions of ease of administration, interviews with Managing Authorities and financial intermediaries provide some more qualitative insights. In general, as reflected in the survey, financial instruments are considered to be harder to administer than grants; this is consistent with findings in other studies.[153] However, a key issue concerns the ***lack of experience*** among Managing Authorities in dealing with support other than grants.

> "a combination of Cohesion Policy related capabilities must be coupled with financing-banking knowledge and skills. Such a skills mixture can only be built up through implementation experience." (Managing Authority interview)

> "Capacity at all levels, including the EC, is inadequate as the combination of Cohesion Policy implementation and banking experience is rather rare." (Financial intermediary interview)

> "Ensuring the skills mix of Cohesion Policy implementation and banking is a continued challenge." (Financial intermediary interview)

> "Increased requirements on administrative capacity (not only internal, necessity to engage also external actors)" (Managing Authority interview)

> "The main disadvantage is the lack of experience in using FIs and the procedures that have to be followed." (Managing Authority interview)

> "Cons – they are complex, requires highly specialist staff." (Financial intermediary interview).

[153] Wishlade, Michie R, Familiari G, Schneidewind P and A Resch (2016) *Op cit*.

> "Delivering JEREMIE helped to create a pool of experts; however the overall capacity is not very robust yet." (Managing Authority interview)

Among financial instruments, there was generally more confidence about the capacity to deliver *loan* and *guarantee* schemes than *equity* products.

> "Regarding capacity, equity finance is a relatively new phenomenon" (Financial intermediary interview)

> "Guarantee institutions are highly specialised. They have to better understand EU regulations; this challenge is not substantial though." (Financial intermediary interview)

> "We have used FI beforehand as well and that is why we have already enough experience in this field. That is why we were able to open loans and guarantees so quickly." (Financial intermediary interview)

> "Administrative capacity for loan and guarantee finance is adequate generally." (Financial intermediary interview)

Another issue that emerges from the interviews concerns the ***quality of the regulatory framework*** and how that affects the ease of administration of financial instruments as opposed to grants. The regulatory framework is discussed in more detail in 4.10 below where the issue is addressed explicitly. The following remarks were unprompted:

> "Cons of FIs are that the regulatory framework is not yet fully developed. In many cases this results in legal uncertainty." (Intermediate body interview)

> "…the regulatory framework is still better suited to non-repayable grants. This is an obstacle to the successful management of FIs." (Managing Authority interview)

> "lack of adequate regulations (2017-13) has now been replaced by overregulation and the logic of grants management has prevailed in many areas of FI rules (e.g. transaction based audit, monitoring and reporting system) (Financial intermediary interview)

> "the private sector is very sensitive to setting up of clear conditions; however the EU regulatory framework still has not been completely clarified." (Managing Authority interview)

The ***administrative burden*** was generally thought to be higher for financial instruments as opposed to grants. The most frequently mentioned issue relates to the burden on financial intermediaries and final recipients – perhaps comparing the administrative burden related to monitoring and reporting obligations attached to the use of publically-funded FIs, as compared to private sources of finance.

> "A drawback of FIs is that the process required is time-consuming and that it is intensive in coordination tasks." (Managing Authority interview)

> "The main drawback is the administrative burden attached to FIs. For instance, eligibility requirements and audit procedures are problematic." (Managing Authority interview)

> "Grants: easier to implement... once agreed not much work left for MA. FIs: creates more work, e.g. making sure money is paid back, reusing recycled funds etc." (Financial intermediary interview)

"Sometimes it is difficult for the financial intermediary to identify the applicable regulations. This results in the circumstance that financial intermediaries often draft very heavy legal documents in order to be on the safe side. Audit visits are also cumbersome and time consuming."(Financial intermediary interview)

[FIs carry a] "high administrative burden for the intermediary and the final recipients." (Financial intermediary interview)

"It is much cheaper and easier to deliver grant programmes than FIs especially equity funds" (Financial intermediary interview)

However, this view was not universally held and some considered that (certain) financial instruments had advantages over grants in terms of administration, or that the difficulties were overstated.

"Administrative burden is biggest in the case of grants and least in the case of guarantees." (Financial intermediary interview)

"Some experience is required when it comes to implementing instruments but FIs are not as complex as is sometimes suggested." (Managing Authority interview)

Some Managing Authorities also noted that the involvement of financial intermediaries lessened their administrative burden:

"An additional pro is that financial intermediaries helped the marketing of the product through their branch offices." (Managing Authority interview)

In addition, some respondents distinguished different aspects of the administration process, noting that, for final recipients, the process of applying for a financial instrument may be quicker and simpler than applying for a grant, notably where an experienced financial intermediary was involved in administering the FI.

"Speed of administration… …guarantees are administered in one or two weeks" (Managing Authority interview)

"Grants have a higher administrative burden for applicants than FIs" (Managing Authority interview)

Other administrative aspects of FIs were sometimes considered more straightforward than grants:

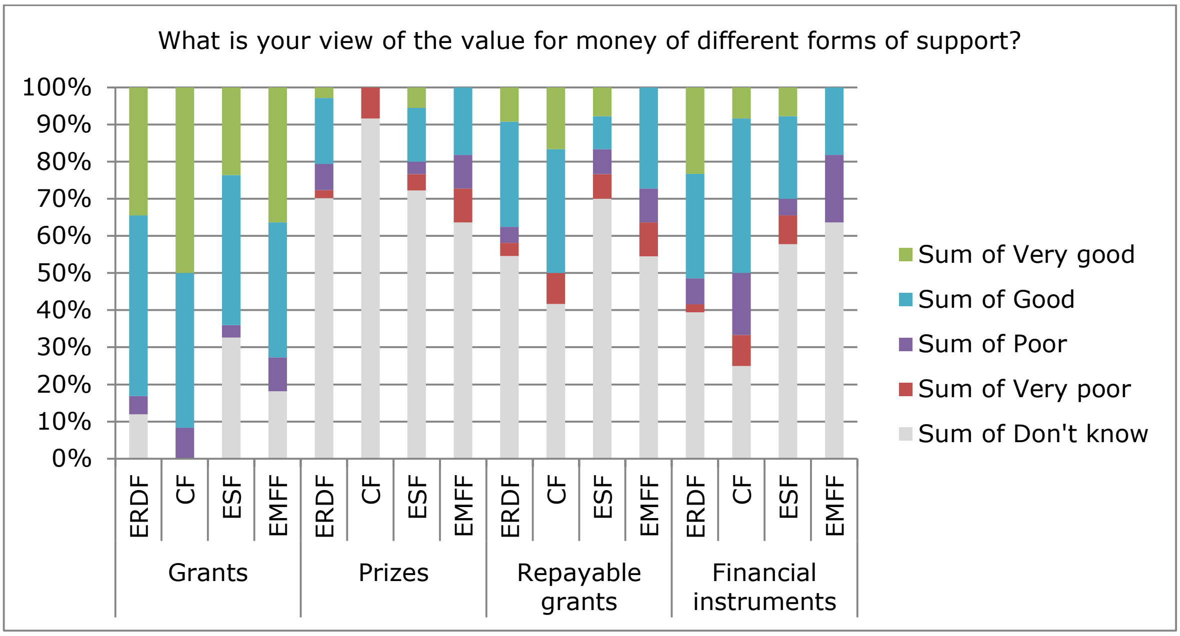
"Quick certification of resources, which is important for achievement of milestones in 2018" (Managing Authority interview)

Last, in spite of the new provisions on phasing of payments to FIs, financial instruments were still felt to be helpful in smoothing financial flows and avoiding decommitments.

4.3. Value for money: how do different forms of support compare?

Value for money has been a growing concern in public policy for many years, and this has led many to question the role of grants to promote economic and social development. Indeed, the notion that financial instruments provide better value for money because sums are repaid and reinvested is one of the key arguments put forward by the Commission for their use. Perhaps surprisingly, then, the survey of Managing Authorities did not bear out this perception (see Figure 4.6). A large proportion of respondents had no opinion on the value for money of repayable grants, prizes or financial instruments, probably owing to lack of experience in their use. However, some respondents perceived that all instruments other than grants offered very poor value for money.[154]

Figure 4.6: 'Value for money' (all respondents, by Fund)

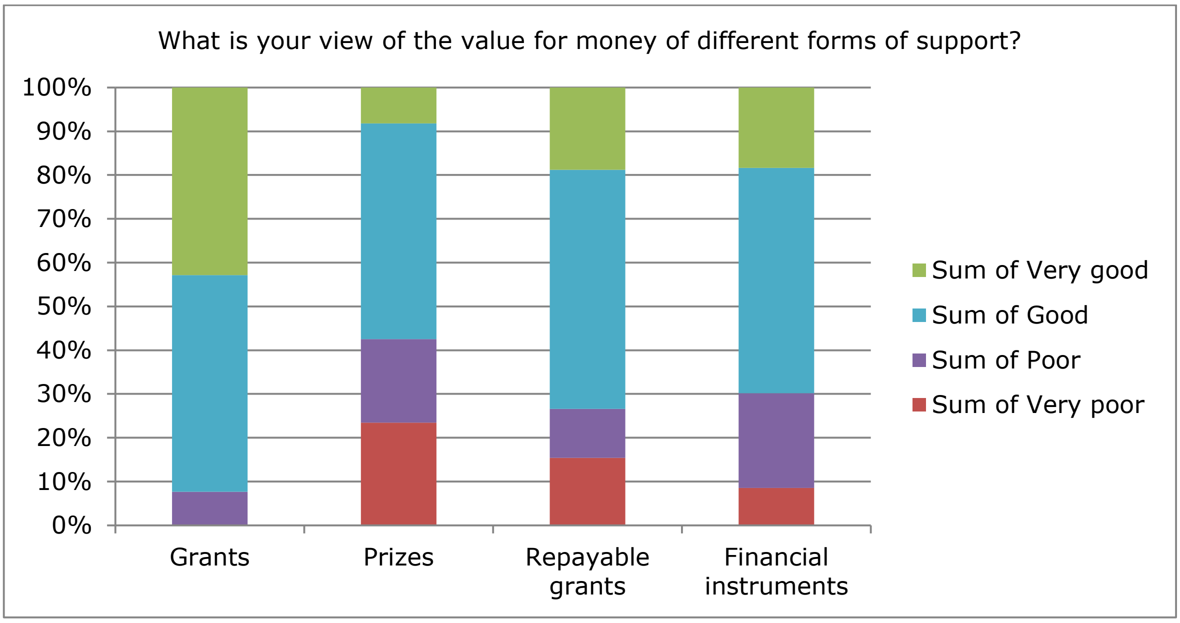


Source: EPRC online survey of Managing Authorities.

Excluding the 'don't knows' from this analysis changes the picture somewhat – see Figure 4.7. On this basis, over 40 percent of those with a view consider prizes to be poor or very poor value for money, but the perception is also fairly negative for financial instruments, where almost 30 percent take this view.

[154] Except in the case of financial instruments for EMFF.

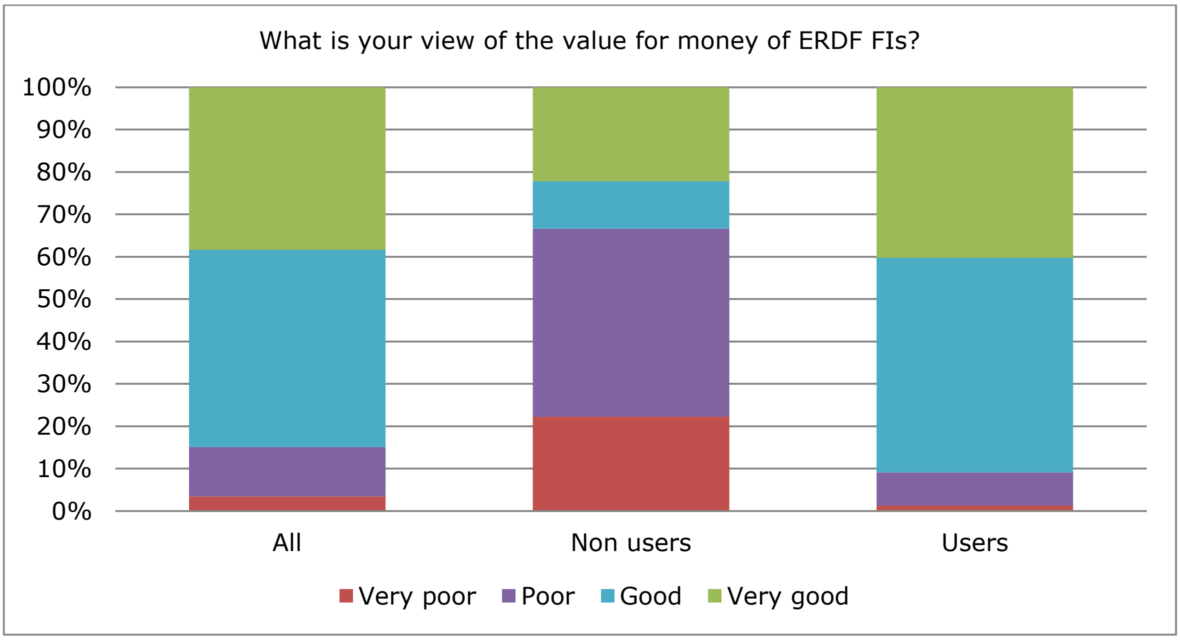
Figure 4.7: 'Value for money' (all Funds, excluding 'D/Ks')



Source: EPRC online survey of Managing Authorities.

Importantly, the survey took account of the views of both users and non-users of financial instruments, and as Figure 4.8 shows, these two groups have different views of the value for money of FIs: ***over 65 percent of non-users of FIs considered that FIs offered poor or very poor value for money, but fewer than 10 percent of FI users shared this view***.

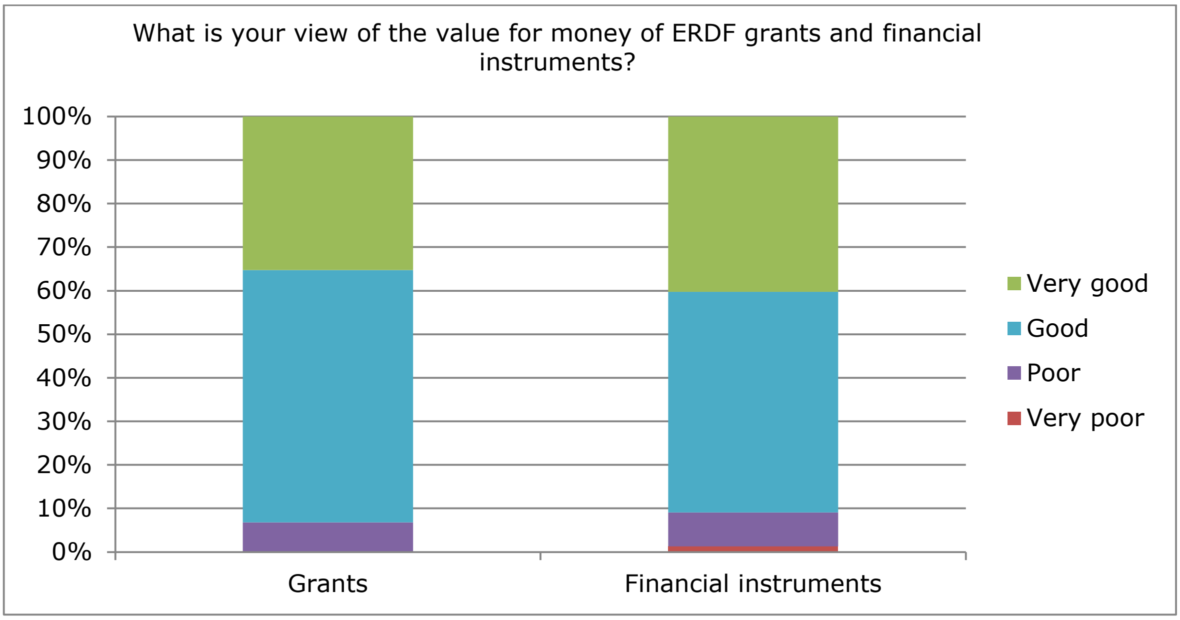
Figure 4.8: 'Value for money' (ERDF MAs, excluding 'D/Ks')



Source: EPRC online survey of Managing Authorities.

Figure 4.9 shows the perceptions of value for money for both grants and FIs among MAs which use FIs. At first sight the outcome may be surprising since the results are broadly similar for the two types of instrument. However, the interviews with Managing Authorities who use both types of instrument make clear the importance of tailoring support to project requirements. In other words, in some contexts, grants may well offer good value for money because the administration costs would be too high if financial instruments were used for the same purpose. In short, *value for money is not inherent in a certain type of support, but is related to the purpose for which it is used.*

Figure 4.9: 'Value for money' (ERDF MAs using FIs, excluding 'D/Ks')



Source: EPRC online survey of Managing Authorities.

Beyond the survey, interviews with Managing Authorities and financial intermediaries provide some further insights into their perceptions of value for money of grant and financial instruments, in particular. The key point that emerges is the ***sustainability*** of financial instruments and, related, the ***ability to support more projects:***

> "From a MA perspective the greatest advantage of FIs is that they are revolving and therefore more can be done with a relatively small pot of money. There is some risk that loans will not be paid back but the estimation is that around 75 percent will be returned for re-investment." (Managing Authority interview).
>
> "From the standpoint of public authorities, FIs have the advantage of reutilising funds and, therefore, a more sustainable policy." (Financial intermediary interview).
>
> "[the key advantage of FIs is] their revolving character, allowing for directing resources to higher number of beneficiaries" (Managing Authority interview).

It is worth noting that in 2007-13 the importance of returns / the 'revolving effect' tended to become more prominent on the agenda of MAs as the programme period progressed. 'Revolving' of funds does not tend to happen until later in the period (as loans are repaid/equity investments mature) and few MAs had an explicit strategy upfront for dealing with (or reporting) revolving funds. Also, attention in the earlier years of the programme period was heavily focused on the administratively demanding set-up and implementation stages of FIs. As returns started to be received (and re-invested), this aspect of FIs was increasingly valued.[155]

Also perceived to be key is the scope to ***attract private sector resources and expertise*** and increase the ***leverage*** of the intervention:

[155] Wishlade, Michie R, Familiari G, Schneidewind P and A Resch (2016) *Op cit*.

> "Possibility to obtain additional resources for energetic savings due to potential agreement with the EIB on possible investment." (Managing Authority interview).

> "They give the option of using the private sector to assist, using their skills in assessment and due diligence so you don't lose as much. Use of FIs builds capacity for recipients. (Managing Authority interview).

> "The main advantage is that access to finance is improved by leveraging private resources." (Managing Authority interview).

That said, respondents also noted that the value for money of financial instruments depended on the ***economic context:***

> "In the times of low interest rates, limited possibility of providing much preference in cost, limited interest of ultimate beneficiaries." (Financial intermediary interview).

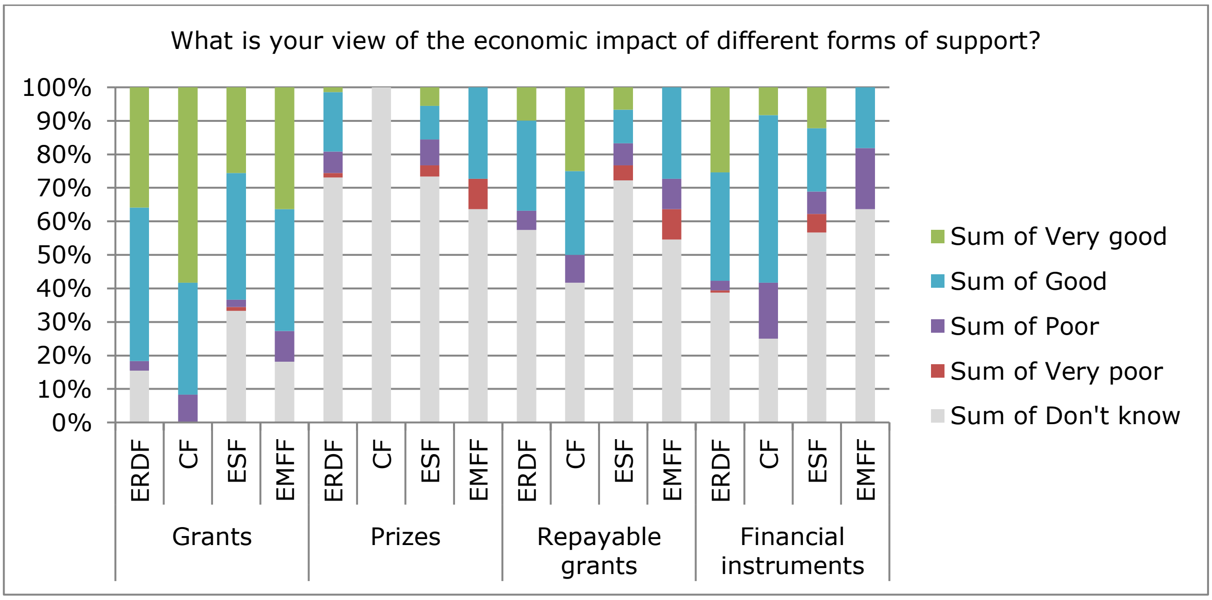
As well as having the required ***critical mass*** in relation to ***management costs*** and fees:

> "…critical mass to reach economies of scale is important to be able to support the high management costs associated with FIs." (Managing Authority interview).

4.4. Economic impact: how do different forms of support compare?

Among the arguments for financial instruments is that their economic impact can be greater not only because funds are recycled and support more projects, but also because the use of repayable funding can improve project quality.[156]

Figure 4.10: 'Economic impact' (all respondents, by Fund)

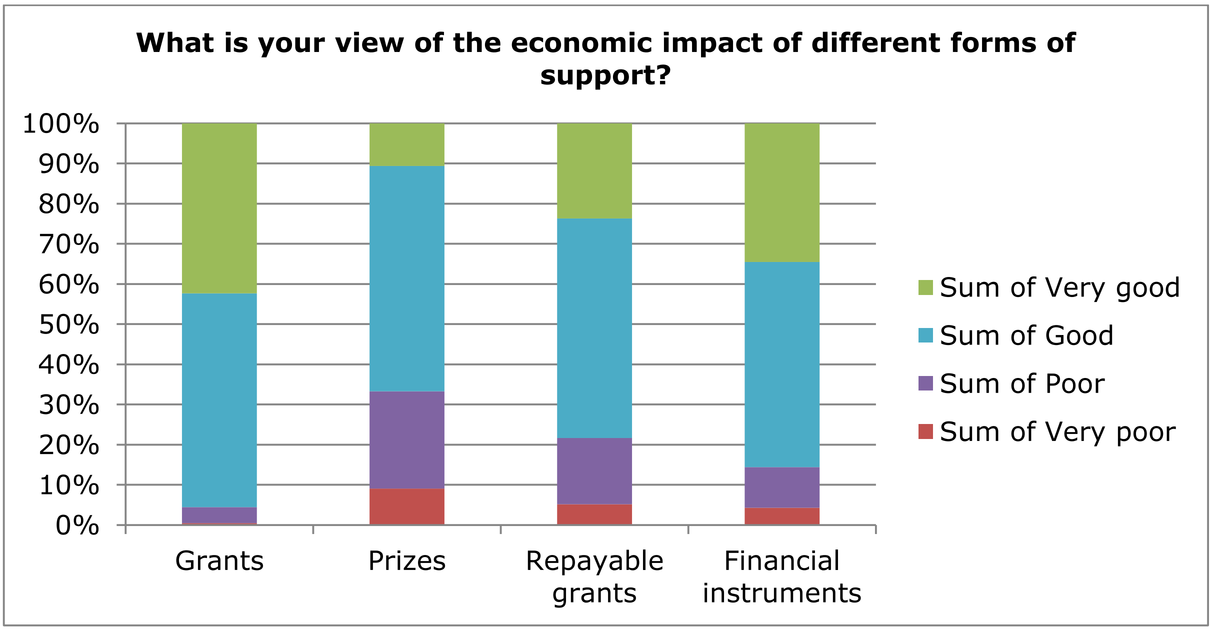


Source: EPRC online survey of Managing Authorities.

Figure 4.10 suggests that Managing Authorities harbour doubts about the economic impact of *all* types of support. However, except in the case of grants, most Managing Authorities 'don't know' about the economic impact.

[156] These answers are based on MAs' perceptions of 'economic impact', which was not defined in the survey question.

Figure 4.11: 'Economic impact' (all Funds, excluding 'D/Ks')

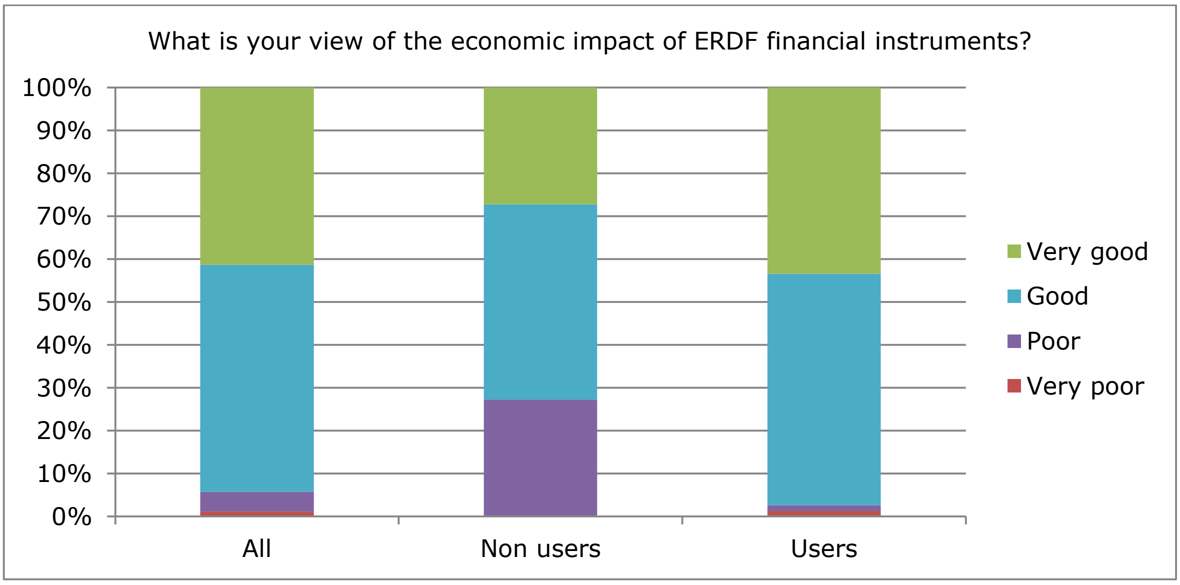


Source: EPRC online survey of Managing Authorities.

Taking account only of those with an opinion, Figure 4.11 suggests that grants are considered to have the highest economic impact – with over 90 percent considering the impact to be 'good' or 'very good', compared with under 70 percent in the case of prizes.

Figure 4.12 considers only ERDF MAs, but distinguishes between those using, or planning to use, financial instruments, and 'non users'. This shows that **over 97 percent of those using FIs consider that the economic impact financial instruments is good or very good**, compared with just over 70 percent of 'non-users'. It is, however, important to note that the majority of non-users expressed no opinion. Somewhat curiously, about two percent of those MAs planning to use FIs considered their impact poor or very poor.

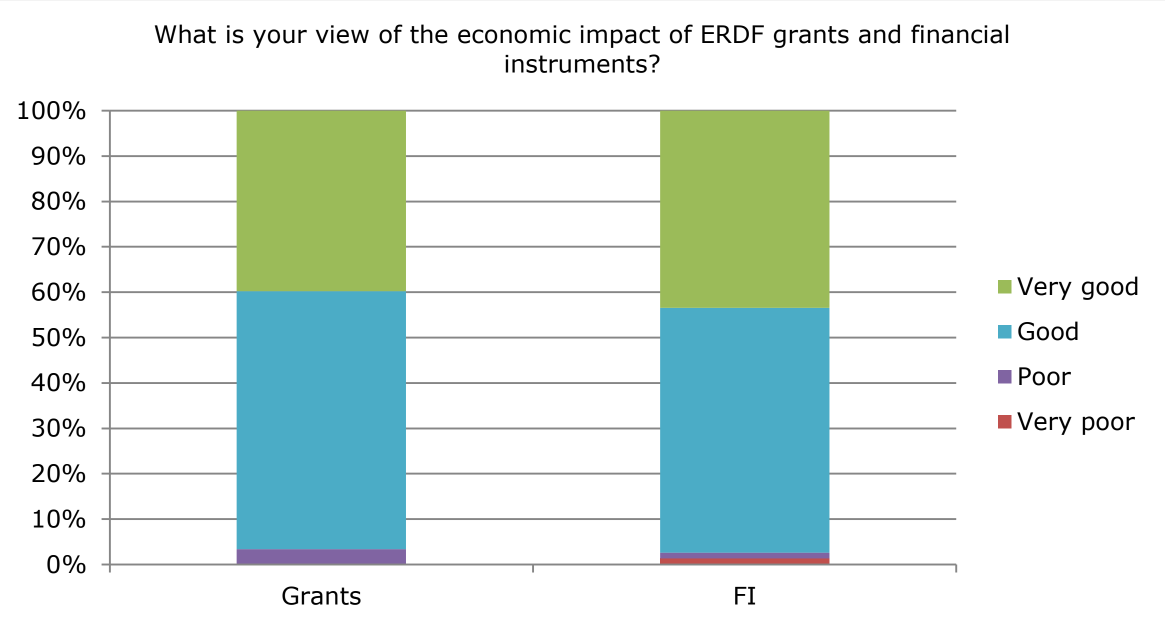
Figure 4.12: 'Economic impact' (ERDF MAs, excluding 'D/Ks')



Source: EPRC online survey of Managing Authorities.

Figure 4.13 compares perceptions of grants and financial instruments, but only among ERDF MAs that are users of financial instruments.

Figure 4.13: 'Economic impact' (ERDF MAs using FIs, excluding 'D/Ks')



Source: EPRC online survey of Managing Authorities.

Similar to perceptions on value for money, there is not a great deal of difference between the two, with a slightly higher proportion considering FIs to have a 'very good' economic impact. The reasons underlying this are not clear from the quantitative data alone. However, it may be related to different forms of support being tailored to the needs of the OP, and both forms perceived as being capable of delivering equally good economic impacts in relation to the targets for which they are designed.

Interviews with Managing Authorities and financial intermediaries suggest that FIs are perceived to have economic impacts on several levels. At the micro level, a large number of respondents note that FIs have a positive impact on the ***competitiveness of financial recipients*** or were more likely to attract ***high quality applicants*** than grants:

> "Final recipients of FIs are more likely to become more competitive and gain easier access to commercial loans in future" (Managing Authority interview)
>
> "Use of FIs builds capacity for recipients. If you don't have a track record then banks won't look favourably on you but you can give your credit rating a boost using ERDF FIs successfully, then move on to get money commercially." (Managing Authority interview)
>
> "Prepares projects for commercial funds" (Managing Authority interview)
>
> "FIs foster business-like thinking" (Financial intermediary interview).
>
> "There is more scope to provide expert advice alongside FIs than there is for grants" (Managing Authority interview)
>
> "When using FIs additional assistance, such as experts' advice can be provided." (Managing Authority interview)
>
> "Relatively easy to decide if a project is good – the capacity of a project to repay aid is a sign of that." (Managing Authority interview)

Financial instruments were also felt to have ***wider economic benefits***. These included the multiplier effect arising from the reinvestment of returned funds and the absence of deadweight perceived to be present in the use of grants.

In addition, respondents also pointed to the ***benefits for financial markets***. Some respondents noted that ESIF FIs help develop the private financial sector, and diversify it, especially into risk capital (even in countries with relatively developed financial markets overall, as these markets tend to be geographically concentrated). One Managing Authority noted that FIs could be co-financed from national pension funds, which would otherwise be invested in foreign markets.

Last, several respondents cited the capacity of FIs to have greater economic impact for less outlay:

> "FIs enable public authorities to carry out policy actions of high impact with few resources." (Managing Authority interview)
>
> "More important environmental effects for the same amount of resources" (Managing Authority interview)

4.5. What factors influence the choice of financial product in OPs using FIs?

The term 'financial instrument' has become a 'catch all' for forms of support that are repayable, unlike grants. In practice, however, this term encompasses a variety of forms which may have little in common with one another. By convention, financial instruments are divided into three groups:

- ***Loans,*** or debt - these may be provided directly by Managing Authorities or through financial intermediaries.
- ***Guarantees*** – where capital is wholly or partially secured in the case of a default. These may also be provided directly by Managing Authorities and aim to encourage commercial lenders to provide capital to borrowers lacking adequate collateral or perceived to be too high risk.
- ***Equity*** – where a holding or share is taken in the capital of a firm. Equity or venture capital cannot be implemented directly by Managing Authorities.

In practice, there are many variants on each of these forms in relation to the terms on which they are offered, the mechanisms through which they are implemented and the extent to which they are combined. For example, mezzanine finance can be considered a hybrid of debt and equity, and may be structured as a loan to the final recipient or as a shareholding in the final recipient. Microfinance, conventionally used for start-ups especially to encourage entrepreneurship among marginalised groups, often takes the form of guarantees and loans in combination. Guarantees may be offered directly to the borrower, or in the form of counter guarantees to smaller lenders.

Box 4.1: The use of equity FIs in ESIF programmes

In 2007-13, the vast majority of products disbursed to final recipients via FIs were loans (either awarded directly as loans or supported through the provision of guarantees). Equity FIs are those which involve the investment of capital in a firm, either directly or indirectly, in return for total or partial ownership of that firm.

The use of equity FIs in 2007-13 was concentrated in a few countries (e.g. DE, PT, SE and the UK). By the end of 2015, 5,505 equity and quasi-equity investments had been made in 2007-13 OPs, with a total value of €2,372 million, out of which €1,351 million was from the Structural Funds.[157]

Equity FIs tended to be used to support innovative firms and business start-ups with high growth potential (and therefore high returns), but also high risk (and potentially high losses). According to the ex post evaluation of FIs, equity FIs attracted higher levels of private sector participation than other instruments, but performance was difficult to assess as few exits had yet taken place (most equity FIs were established for a set period of 10 years). However, there were clear signs of ERDF support having helped the creation of a venture capital market in areas where it was poorly developed.[158] While most of the equity FIs in 2007-13 were regional in scope and comparatively small, size did vary greatly, ranging from €390,135 (Poland) to €85.1 million (Germany).

In 2014-20, planned OP contributions to equity FIs amount to c.€4,700 million, around 22 percent of the total planned allocation to FIs. This represents a doubling in the planned use of equity instruments, although, as with all FIs, the actual amounts committed will vary depending on the results of the ex ante assessments and other factors.

Historically, there is less experience with implementing co-funded equity FIs, and what there has been is concentrated in a few Member States. A number of barriers to further uptake of equity FIs exist - equity is a 'niche' product and will only ever be attractive to a very small proportion of high growth firms in any given Member State or region. MAs have found that selection of projects for equity investment takes longer and is more expensive, due to the in-depth due diligence required. Also, venture capital markets in target regions/Member States may be poorly developed and lack the required capacity in terms of fund management.

Source: EPRC Case study research – see Annex 1.

Interviews with Managing Authorities showed that a number of factors determined the choice of financial product. Chief among them, not surprisingly, was the ***outcome of the ex ante assessment.*** This highlights the importance of a new compulsory element in the 2014-20 regulations. Decisions on financial products could not be taken until the ex ante assessment had been complete, providing the evidence required. This could differ from what had originally been envisaged in the OP (potentially requiring a programme modification to be made).

> "From FIs only loans are proposed. The ex ante assessment recommended also some other types of FIs. The final choice was influenced esp. by foreign experience, experience of responsible persons of specific interventions, knowing well situation of the market." (Managing Authority interview).

> "The choice for the financial products offered was the result of the ex ante assessment. The market environment and the capabilities of the Ministry of Finance were taken into account." (Managing Authority interview)

> "The main factor influencing the type of FI made use of was the advice from consultants and the results of the ex ante evaluation." (Managing Authority interview)

> "The financial product was chosen as a result of the ex ante assessment's conclusions. In addition, the EIF offered guidance regarding the most appropriate type of financial product." (Managing Authority interview)

> "Use of different financial products depend on the development stage of an enterprise (new or growing), operational focus (innovative or life style business), its needs, purpose of investment, collateral requirements, costs of FI, etc. Before the ex ante assessment was conducted the [MA] had a vision for using particular financial

[157] European Commission (2015) Summary of data on the progress made in financing and implementing financial engineering instruments co-financed by Structural Funds, September 2016.

[158] Wishlade F, Michie R, Familiari G, Schneidewind P, Resch A (2016) *Op cit*.

products for the OP, which were further analysed in detail in the ex ante assessment. Aspects of the ex ante assessment, as well as previous experience implementing FIs were taken into account, when drafting OP.... The decision on particular financial products was taken after negotiation process with the Commission." (Managing Authority interview).

"The main driving factor was the ex-ante assessment - advice from consultants responsible for preparation of this document. Additionally, prior experience in applying FIs. Finally, decisions to concentrate mostly on supporting capital investments (VC investment formats) - financing of early stages." (Managing Authority interview).

In addition, ***experience*** or ***administrative capacity*** of the Managing Authority also played a significant role for many:

"The main factor that influenced the choice of financial product was prior experience. "(Managing Authority interview).

"…factors: previous experience, conservative approach" (Managing Authority interview).

"experience from previous periods." (Managing Authority interview).

"secondary (after type of products were decided upon), experience and capacities of involved institutions in final design of financial products." (Managing Authority interview).

"When choosing between lending and equity schemes, on the consideration of 2007-13 experience, preference of the MA goes for loans; they are smaller size, more straightforward to manage and bring about less audit risks." (Managing Authority interview).

"The choice of instrument has been driven by the ex ante assessment taking in to account what has worked in certain areas before." (Managing Authority interview).

In some cases the type of financial product was ***determined at the EU level***:

"The ESF FI implemented is a facility put in place by the Commission and managed by the EIB. This has resulted in great advantages, mainly because the Commission provided certainty on the programme and because the EIB provided management know-how. If the FI would have been designed by the Intermediate Body, the process would have been much more cumbersome." (Intermediate body interview,).

In other cases the choice was based on ***specific objectives*** or ***demand***:

"…opted for a venture capital fund, mainly given the fact that it can attract private resources. The revolving nature is not specific to venture capital but it has motivated the choice for FIs. … a venture capital fund has a significant value-added, given the needs of the region." (Intermediate body interview).

"The ministry has traditionally offered loans (matched with non-repayable aid) and guarantees. Microfinance is less suitable for centrally coordinated measures. Regarding equity one of the limits encountered is the lack of demand." (Managing Authority interview).

"…opted for not using loan and guarantees since they offer less value-added for the beneficiaries in the region than venture capital financing possibilities." (Managing Authority interview).

4.6. Do different types of support compete and if so, what drives this?

The relationship between different forms of support is an important one. Unless the various instruments are appropriately tailored to meet policy and market requirements, and dovetailed with one another, there are risks that measures compete, overlap or leave some needs unmet.

Some respondents considered that there was ***no competition*** between different types of support, at least in their own programmes, though sometimes this was simply because forms other than FI are not offered, or because programmes have been shaped to ensure different forms of support work alongside one another.

"Different forms of support are complementary to each other. In the case of FIs - beneficiaries can receive whole amount of financing, when starting the project… which needs to be repaid, but in the case of grant - beneficiary needs to attract co-financing and pre-financing, which may need to be repaid in case of failure. Therefore, attractiveness of grants versus FI is questionable…. specific support criteria are being designed, which determine if the project can receive FIs or grants. Competitiveness of the project determines which form of support should be used in each case. In this respect different forms of support can't be in competition with one another."

"In relation to TO9 there is no competition as support is only offered through FIs"

"The current division of financing forms is done in a way to make sure the instruments are not in competition each to the other. From the point of view of final recipients grants are more attractive, but - basically - they are not offered in TO 3 which is the most important objective in which we plan to use financial resources."

"The OP is designed in such a manner that FIs and grants are not compatible. There is no competition."

In the main, Managing Authorities considered financial instruments and other forms of support to ***complement*** one another, and some had explicit mechanisms to ensure this.

Box 4.2: Mechanisms to ensure complementarity of forms of support

"The MA endeavoured to set up the implementation system so that grants and FIs were complementary (ex ante assessment was very helpful). The MA uses mechanisms:
(1). assessment of projects according to internal rate of return at the level of projects (used for projects focused on energy savings. This rate is assessed by independent auditor. The beneficiary can run for credit in all cases but the project is eligible for grants only in case that the internal rate of return is below a predefined level)
(2). regional mechanism (e.g. for technologies - technologies are supported via FIs in all regions and grants are available only in regions with specific problems)."

Source: Managing Authority interview.

Other were less explicit in their explanations, but made clear that ***steps had been taken to ensure complementarity***, especially in the light of experience in 2007-13.

"No, the different forms of support are designed to be in complement with one another". (Managing Authority interview)

"No. This has been made impossible, because the whole process of setting-up FI is participatory (with regions and the Ministry for Economic development). Firms themselves see these instruments as complementary (this emerged from interviews and focus groups).” (Managing Authority interview)

“grants and FIs can be combined. Therefore, they complement each other” (Managing Authority interview)

“… this was a common problem in the 2007-2013 programming period, where ERDF and other types of support often were cannibalised. In the 2014-2020 programming period this issue will be resolved by the ex ante assessment.” (Managing Authority interview)

“From the entrepreneurs' point of view grants could be competing with FIs, as grants are cheaper source of funding. However, different FIs are focused to different objectives and, therefore, they don't overlap and provide an opportunity to select the most appropriate type of support for a particular project. Entrepreneurs can select the most appropriate form of FIs taking into account his/hers needs and possibilities.” (Managing Authority interview)

“Specialised calls are useful…[to prevent competition between forms of support]. The risk is over-specialising that usually results in a markedly narrow scope of potential beneficiaries. Ideally, different forms of support could be offered for companies which have achieved different phases in the project lifecycle. Disbursement of grant assistance for R+D+I projects may have reduced, hopefully temporarily, the interest in applying for loan finance.” (Managing Authority interview)

Other Managing Authorities take the view that ***different forms of support do compete***. In part this owes to overlap in the objectives of the measures concerned, but is also due to the preference of final recipients, who often continue to prefer grants. Some respondents also noted that FIs were potentially disadvantaged by the amount of time they took to establish.

“To some degree the FIs are considered to be in competition with grants, they are more risky …environment is not used to this form of the assistance… time disadvantage of the FIs – the EC does not clarify sufficiently all the conditions and that makes the MAs start with grants.” (Managing Authority interview)

“In relation to TO4 there can be some competition but it mainly depends on the strength of the business case of the project whether a project would be considered for grants or FIs.” (Managing Authority interview)

“When similar activities are financed using grants and FI, grants reduce the attractiveness of the financial instruments.” (Managing Authority interview)

Although there is ***often a presumption that grants would be more attractive*** to final recipients, this is not always thought to be so.

“there is also some path dependence among final Recipients, as they prefer grants rather than FIs” (Managing Authority interview)

“beneficiaries would mostly opt for FIs since procedures are significantly reduced in comparison with grants. For grants you need specialized consultants, not just for application but also for the implementation and reporting. For FI, loans for example, beneficiaries approach banks in ordinary fashion as if no EU funds are concerned. FIs are complicated to set-up and monitor implementation but only for involved institutions, once launched FIs are quite fast and simple for final recipients.” (Managing Authority interview)

> "Not only different but the same forms of support may compete. Project promoters optimise and always look for finance with the most favourable terms. Long-term grant beneficiaries are now shifting towards combined products (grant + loan). Also, an SME can apply for support under various TOs; they will scrutinize price and administrative burden and are likely to devise their application to fit into the scheme with the lowest costs and simplest administration. Pricing helps the elimination of competition, e.g. the interest rate under TO3 related lending schemes is at 0% while the interest rate of the loan element of the combined product under the same TC is 2,5%. Grant rate is to be maximised, probably around 30% for the SME combined product. Early repayment is now penalised to exclude project promoters who want to access grants through the scheme and who are actually in no need of a loan." (Managing Authority interview)

Last, although the emphasis on respondents was on grants and FIs, ***competition is not limited to grants and FIs***:

> "Experience with equity investors in the previous period revealed potential competition between equity and loans, too. Equity funds diversified their portfolio as a natural way to reduce the relatively high risk they bear. Consequently, these funds also undertook investments that could have proven bankable should the company have approached a bank." (Managing Authority interview)

Box 4.3: What drives competition between different delivery modes?

There are clearly risks that different forms of intervention that target the same or similar activity can overlap or undermine one another. The key issues in relation to competition between financial instruments and other modes of intervention include:

- The need for grants and FIs, if both exist, to have a different focus. For example, grants to support general investment by SMEs could readily be substituted by loans; if the two co-exist, there is likely to be a preference for grants.
- The need for grants to target investments where a clear incentive effect is required so that intervention alters the behaviour of the recipient – for example, to undertake a risky innovation project that would not have happened otherwise.
- The need for applications for FI support to be no more complex than those for grants.

The need for FIs to be up-and-running early in the programming period.

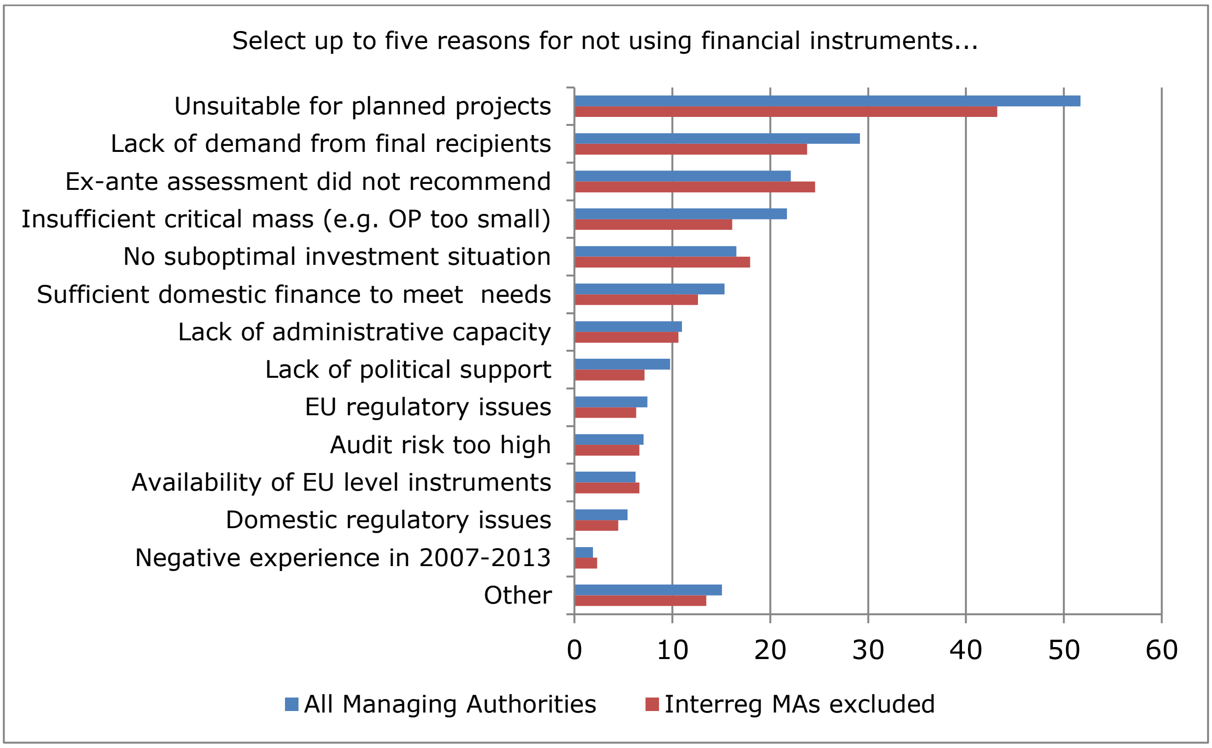
Competition may also be present among guarantee mechanisms and or loans, depending on the coverage or interest rate, and there is some evidence of perceived competition between ESI Fund co-financed FIs and those funded through EFSI. This is discussed in more detail in Section 5 below.

4.7. What underlies decisions *not* to use financial instruments?

Some Managing Authorities do not plan to use FIs at all, whereas others use or plan to use them under some, or even all, Thematic Objectives. As mentioned earlier, several Member States do not use co-financed FIs at all and there are some MAs that have ceased to use FIs in 2014-20, but did in 2007-13. Some of these are presented as a case study (see Annex 1).

The online survey of Managing Authorities sought to understand why financial instruments had not been used. For each Thematic Objective where FIs were not planned, Managing Authorities were asked to indicate up to five reasons for this. Figure 4.14 shows that, across all TOs, the single ***most important reason for not using FIs is that they are deemed 'unsuitable for planned projects'***.

Figure 4.14: Reasons for *not* using financial instruments



Note: (i) Where Managing Authorities were not using financial instruments for a given Thematic Objective, they were invited to select up to five reasons why not. (ii) Figures refer to % of respondents citing the reasons above (iii) An ex ante assessment for FIs may or may not have been carried out; if an ex ante assessment has been carried out, there will be some overlap between categories.
Source: EPRC online survey of Managing Authorities.

Figure 4.14 shows that the outcomes differ slightly among Interreg MA authorities. These account for a significant proportion of non-users of FIs (no Interreg respondents to the survey proposed to use FIs). These outcomes suggest that among Interreg OPs, lack of suitability for planned projects, lack of demand from final recipients and insufficient critical mass are more important reasons for not using FIs than for OPs as a whole.

Figure 4.15 breaks this down by TO (excluding Interreg OPs from the analysis). This shows that while 'unsuitable for planned projects' is the most important reason across all Thematic Objectives, this is not the case for TO1 (research development), TO3 (SME competitiveness) or TO4 (low carbon). The outcomes for TO3 and TO4 are interesting as these are areas where FIs were typically used in 2007-13.

For TO3, the most important reasons for not using FIs are:

1. 'lack of demand' from final recipients (39 percent)
2. = 'unsuitable for planned projects'; 'insufficient critical mass'; 'lack of administrative capacity' (26 percent each)

In the case of TO4 (low carbon economy), the most important reasons are:

1. 'lack of demand from final recipients'; (30 percent)
2. 'insufficient critical mass' (25 percent).

Although 'unsuitability' scored highly in both TO3 and TO4, these scores are low compared to other TOs, reflecting the fact that FIs are used more for these policy areas than others. EU regulatory issues appear comparatively important for not using FIs under TO3, as does 'administrative capacity' (also for TO4).

In general, 'negative experience in 2007-13' does not score highly as a reason for not using FIs in 2014-20, but six percent of MAs cite this as a reason for not using FIs under TO4 in the current period.

Figure 4.15: Reasons for *not* using financial instruments by Thematic Objective

	Total	TO1	TO2	TO3	TO4	TO5	TO6	TO7	TO8	TO9	TO10	TO11
Unsuitable for planned projects	43	28	45	26	19	43	48	43	44	52	52	67
Ex-ante assessment did not recommend FIs	25	34	28	4	17	23	23	40	19	26	25	24
Lack of demand from final recipients	24	30	26	39	30	17	32	25	14	20	20	19
No suboptimal investment situation	18	15	19	17	17	15	16	18	19	19	21	19
Insufficient critical mass (e.g. OP too small)	16	21	14	26	25	15	18	3	19	15	12	14
Sufficient domestic finance to meet finance needs	13	21	12	17	21	15	10	5	9	13	10	10
Lack of administrative capacity	11	9	7	26	21	9	11	3	13	10	9	5
Availability of EU level instruments	7	17	2	9	6	2	0	5	10	11	5	5
Lack of political support/consensus	7	2	7	4	8	6	6	10	6	8	7	24
Audit risk too high	7	8	3	13	6	4	5	3	11	10	7	0
EU regulatory issues are an obstacle	6	17	7	22	8	4	5	3	3	5	4	0
Domestic regulatory issues are an obstacle	4	9	7	9	9	2	5	3	0	2	4	0
Negative experience in 2007-2013	2	6	0	0	6	2	2	3	3	2	1	0
Other	13	13	12	17	17	11	13	18	17	13	10	10

Note: (i) Where Managing Authorities were not using financial instruments for a given Thematic Objective, they were invited to select up to five reasons why not. (ii) Figures refer to % of respondents citing the reasons above, but excluding Interreg MAs. (iii) An ex ante assessment for FIs may or may not have been carried out; if an ex ante assessment has been carried out, there will be some overlap between categories.
Source: EPRC online survey of Managing Authorities.

'Other' reasons were mainly that the ex ante assessment had not yet been finished, though some further points are noted:

> "We prefer to have total control of the funds" (Managing Authority survey response)
>
> "Tighter controls on monitoring and reporting than for other forms of assistance." [presumably referring to the administrative burden] (Managing Authority survey response)

Interviews with Managing Authorities confirmed the reasoning given in the surveys, but some yielded more detailed insights. Some of these were quite ***context specific***, as Box 4.4 shows.

Box 4.4: Impediments to using FIs for water quality and low carbon projects

Within the intervention focused on improving of water quality loans or equity were recommended in the ex ante assessment ….the MA decided not to use the FIs here for many reasons, especially: less experience, risks of low absorption capacity (for this form of assistance), political reasons (fear of increasing of water rates and sewer rates as a result of market setting of projects). The decisive factor in case of intervention focused on decreasing of emissions from heating consisted in administrative burden (and management costs) in comparison with capacity of intermediary organisation and in the fact that the rate of grants was increased and the loans would be too small.
Source: Managing authority interview.

For ***Interreg***, there are also specific impediments:

> "The biggest issue is the kind of projects undertaken and that they are not income generating usually. Also, the amounts – you need a minimum amount – a critical mass to run a financial instrument and ETC programmes are too small…. [there is a clash] a set of indicators meant for a different kind of project. If the COM wanted ETC programmes to use FI it would have to impose it and then provide a mechanisms where ETC programmes would contribute to an EU level fund with money from the programme". (Managing Authority interview).

Other constraints were related to the nature of the beneficiaries, implying, for example, that ***large undertakings and public institutions might not be suitable targets*** for FIs:

> "complicated rules and type of beneficiaries and their expectations – e.g. high-speed access to internet (rules very complicated already for grants, beneficiaries are big companies)." (Managing Authority interview)

> "FIs are considered as a very useful form of support, but not feasible for certain types of projects or type of beneficiaries. For instance, it's very hard to use FIs for public institutions support" (Managing Authority interview)

> "Most of OP's TOs are related to improvement of public infrastructure and investing in social objectives, which wouldn't be appropriate for using FIs." (Managing Authority interview)

Past experience, especially in relation to TO4, is also relevant, a finding from the interviews that is consistent with the online survey:

> "There were some attempts to implement FIs in TO 4 but the experiences have often been negative." (Managing Authority interview)

> "The possibility of implementing a FI in TO4 for energy efficiency was considered. However, this type of support is carried out by a regional agency already and the possibility was discarded. In addition, the experience with JESSICA in the 2007-2013 programming period has not been satisfactory." (Managing Authority interview)

> "The possibility of implementing a FI for energy efficiency in TO 4 was considered. However, that idea was discarded since [the regional development agency] has still limited experience with FIs and operational risk would be too high." (Managing Authority interview)

The interviews also revealed that Managing Authorities ***considered the possible use of FIs under TO1 (R&D&I) to be challenging***:

> "FI preparations under TO1 have quickly revealed the particular capabilities required, including the need to involve highly specialised experts in various phases of

implementation (starting from the appraisal of the applications).” (Managing Authority interview)

“TO1 - extremely low levels of investments in R&D in both private and public sector, potential beneficiaries should be motivated to invest more with grants, since no one will take a debt instrument for investment in R&D when return on investment is not guaranteed” (Managing Authority interview)

“…grants are important for research based projects, renovation of commercial buildings, etc. Grants stimulate faster and larger scale activities in those areas where financing isn't accessible. Using FIs wouldn't be appropriate in such cases. In addition, it is essential to introduce financial instruments in line with the market practice, therefore FI are not implemented under TO1 due to sectoral restrictions.” (Managing Authority interview)

“Using FIs for thematic objectives where no such instruments have been employed before is a major challenge. Problems occurred at a fairly early stage, in the absence of experience, policy planners could only provide limited inputs for FIs. Absorption capacity for new products is often a dilemma, e.g. could equity resources which are made available for R+D+I be absorbed when equity funds have been traditionally looking for innovative companies anyway.” (Managing Authority interview)

More generally, some respondents ***only considered FIs relevant to some TOs***, notably SMEs and low carbon:

“FIs are not applicable for other TOs, except TO3 and TO4….Main barriers are related to type of project, its scale, as well as type of beneficiary - public persons or entrepreneurs.” (Managing Authority interview)

Other concerns were more general, notably ***practical or administrative and capacity considerations,*** including loss of control and coordination problems, and the cost of conducting an ex ante assessment. On capacity:

“missing experience in some areas (e.g. microloans for social enterprises).” (Managing Authority interview)

“The main reason for not using FIs is the lack of experience of public authorities.” (Managing Authority interview)

Regarding ***coordination and control***:

“The main drawback is that with FIs, and especially when financial intermediaries are involved, control over the policy intervention is given up. This has caused some Ministries to opt for grants as opposed to FIs.” (Managing Authority interview)

“The main problem to not go ahead with some plans for FIs are coordination problems between the different regional administrations (...regional government, agencies, etc.), rather than a lack of potential/demand.” (Intermediate body interview)

“it is difficult to articulate a large number of policy interventions. This is an additional reason for not using more FIs.” (Managing Authority interview)

“the main difficulty when designing the FIs was the delimitation with other types of support carried out by other public entities.” (Managing Authority interview)

Last, some respondents mentioned other ***practical issues*** such as those associated with the size of the market, in relation to the size of the region, or the nature of the programme:

> “In the case of equity products there is a problem of target market scope. Being limited to investing only in [the region] makes it difficult to reach an appropriate size. This is also a problem when attracting financial intermediaries, as they tend to focus on target markets larger than [the region].” (Managing Authority interview)

> “We're talking about a cooperation programme with non-EU countries! We already find it hard to deal with ERDF Regulations in the regional programme and we would certainly not launch FIs with non-EU countries which would doubtless lead to controls and checks which would be impossible to verify in countries where administrative practices are far from those in Europe” (Managing Authority, non-user)

4.8. How useful are off-the-shelf instruments and how could they be improved?

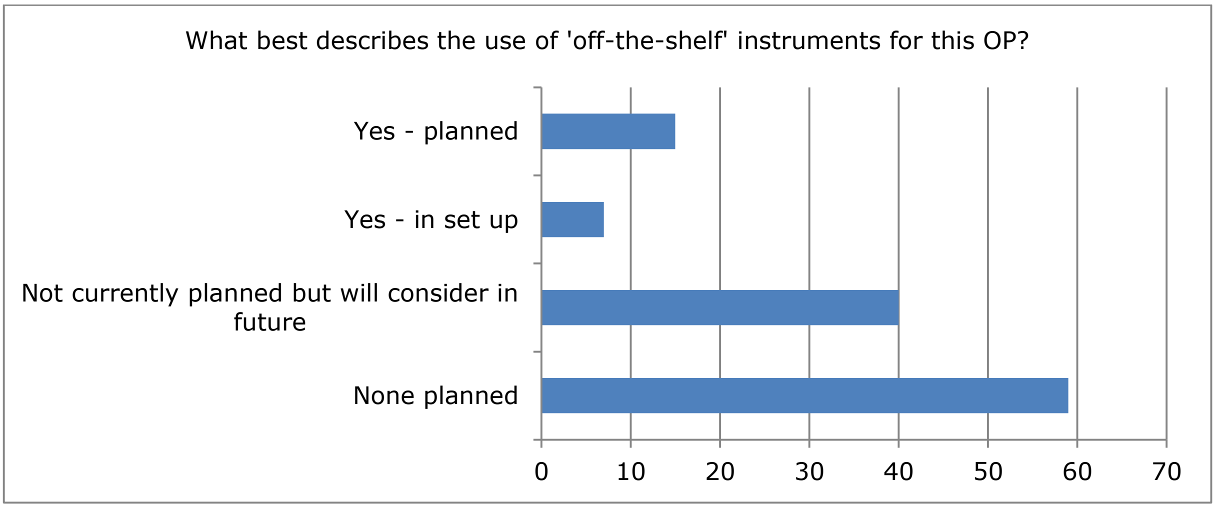
In the 2014-20 regulations, the Commission introduced the option for MAs to use template FIs which comply with standard terms and conditions.[159] The template models are intended to facilitate FI set up; if the template is adhered to, MAs can be assured of the compliance of the proposed FIs across a range of regulatory issues, including selection of financial intermediaries, funding agreements, State aid and management costs and fees. This topic is also explored in a separate case study – see Annex 1.

The first three standardised instruments were made available in 2014 and included a portfolio risk sharing loan, a capped portfolio guarantee, and a renovation loan. These were joined by a further two models in 2016 - a co-investment facility and an Urban Development Loan Fund.

The online survey of Managing Authorities explored the use and planned use of OTS FIs, barriers to their use and scope for improvement.

[159] Commission Implementing Regulation (EU) No 964/2014 of 11 September 2014 laying down rules for the application of Regulation (EU) No 1303/2013 of the European Parliament and of the Council as regards standard terms and conditions for financial instruments; OJ L271; 12.9.2014; Commission Implementing Regulation (EU) 2016/1157 of 11 July 2016 amending Implementing Regulation (EU) No 964/2014 as regards standard terms and conditions for financial instruments for a co-investment facility and for an urban development fund; OJ L192; 16.7.2016.

Figure 4.16: Plans to use 'off-the-shelf' instruments (Managing Authorities planning to use FIs)



Note: 15 MAs reported planned OTS instruments, of which two were SME Initiatives; seven MAs reported OTS FIs in set up, of which one was an SME Initiative.
Source: EPRC online survey of Managing Authorities.

Figure 4.16 suggests that the ***uptake of off-the-shelf instruments has been rather limited***. At the time of the survey, it appeared that 13 OTS FIs were planned and six were in set up (excluding the SME Initiative, which some respondents considered as OTS FIs). However, it did not appear that any of the OTS FIs were operational at that stage. Although uptake of OTS FIs was somewhat limited, the survey also made clear that OTS FIs were of interest in general terms and might be considered for other purposes later. This was confirmed by the Managing Authority interviews, which revealed generally positive views, despite the low take-up. The OTS FIs were described as 'commendable', 'helpful' and 'incorporating best practices'. Their potential to speed up implementation and facilitate management is widely accepted.

> "[The OTS FIs] make the use of FIs accessible to public authorities in a simple way." (Managing Authority interview)

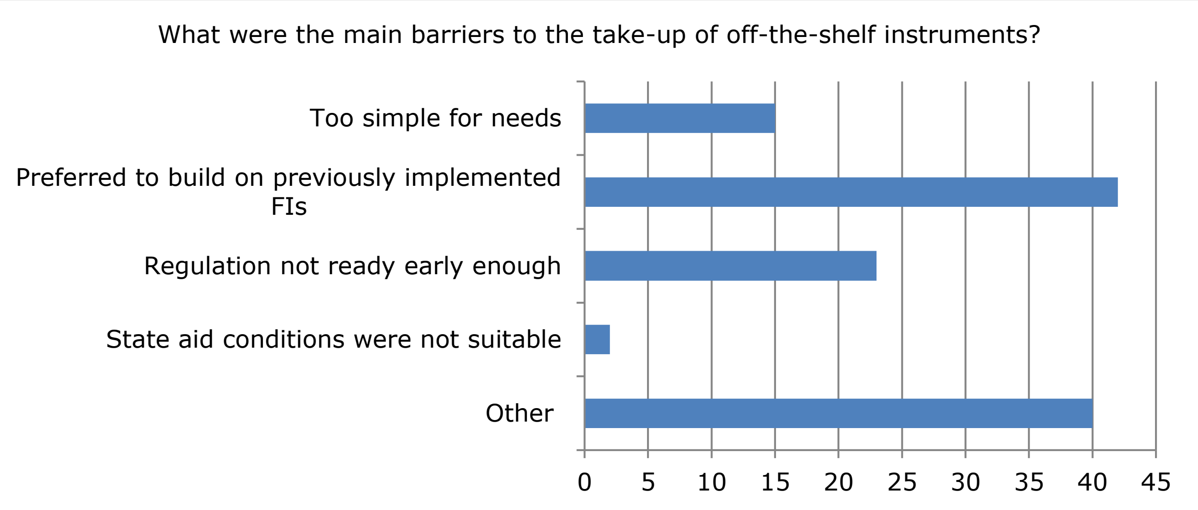
> "[They] remove the vast majority of risks." (Managing authority interview)

> "[They are] especially suitable if an MA does not have prior experience of FIs." (Managing authority interview)

Several MAs stated that they had used the OTS instruments as 'inspiration', to help design final products tailored more closely to their own needs.

As Figure 4.17 shows, the ***main reason for not using OTS FIs was a preference for building on existing FIs.*** This is hardly surprising since many Managing Authorities took considerable time to establish appropriate instruments in 2007-13. Moreover, the available OTS FIs contain no State aid, which means that may be less generous than FIs which MAs have designed themselves and which build on the scope for compatible aid under the GBER.

Figure 4.17: Barriers to take-up of 'off-the-shelf' instruments



Note: MAs planning to use FIs, but not 'off-the-shelf' FIs
Source: EPRC online survey of Managing Authorities.

Managing Authorities also noted that the Regulation had not been ready soon enough for them to establish whether it would be useful, and many considered the mechanisms proposed to be too simple for their needs. However, a large number of MAs cited other considerations beyond those suggested in the survey.

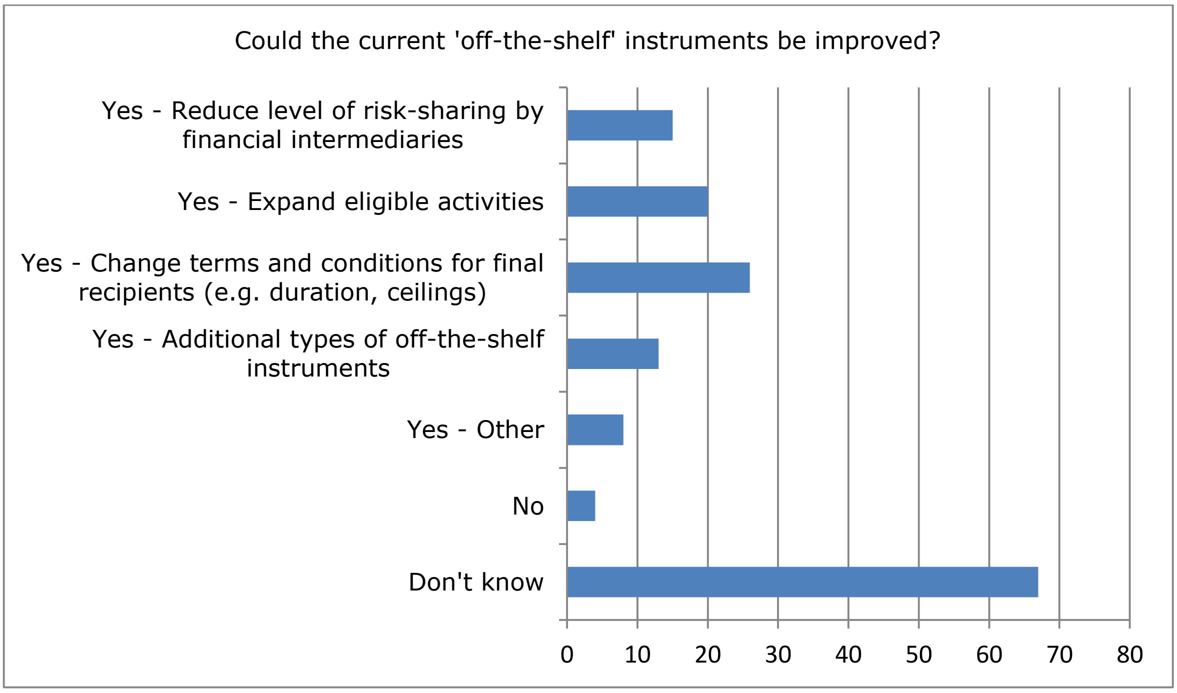
The main reason by far was that the design of the ***OTS FIs available do not meet the current needs of the OP***, for a variety of reasons:

> "The program does not provide support to companies that could benefit from these instruments" (Managing authority interview)
>
> "We planned instruments tailor-made to regional needs" (Managing authority interview)
>
> "All OTS financial instruments are unsuitable because they cover risks which do not exist here." (Managing authority interview)
>
> "Not suitable for our needs" (Managing authority interview)
>
> "Not suitable for the market failures identified" (Managing authority interview)

Another reason for not using OTS FIs was related to ***timing***. Specifically, that the ex ante had not yet been concluded or the type of financial product to be used had not been decided.

Two more specific reasons were also mentioned. First, that the ***OTS FIs require too great a contribution from financial intermediaries*** and are therefore unattractive to them. Second, that ***OTS FIs are inflexible*** – they do not offer scope to adjust or amend elements that do not fit well with the national context. This second point, while understandable at one level, also presents a circular problem since the very purpose of OTS FIs is that, by following the letter of the Regulation, the MA is assured that the FI complies with the relevant State aid, procurement and selection criteria. Clearly this assurance cannot hold if those terms have been amended.

Figure 4.18: Improvements to 'off-the-shelf' instruments (MAs planning to use FI)



Source: EPRC online survey of Managing Authorities.

4.9. What are the key steps in the decision to establish FIs?

The first steps to establishing FIs within an ESIF programme are governed by provisions in the CPR:

- The ex ante evaluation should provide a rationale for the form of support proposed (Article 55(3)(h))
- MAs should indicate planned use of FIs in the OP (Article 96(2)(b)(iii)) (although it can also be introduced after OP adoption)
- an ex-ante assessment must be completed before the MA decides to contribute OP resources to an FI (Articles 37(1)-(2) and Implementing Regulation (EU) 964/2014 Article 3(1)).

Prior to, and alongside these steps, a number of activities can take place which have an impact on whether FIs are established (see Figure 4.19):

1. *Discussions before the OP is drafted* - the use of FIs may be discussed before the OP is drawn up, potentially in parallel with Partnership Agreement negotiations (depending on the procedure in the Member State /region concerned); **high-level analyses** may take place, evaluation results of previous FIs may be incorporated, and discussion take place to inform and develop the approach (even when no FIs are ultimately chosen in the OP).

> "More intensive debate on the form of the assistance appeared before finalization of the OP – when specific objectives were outlined. In 2014, the MA commissioned general analysis of potential usage of FIs and findings of this document were developed in following discussions." (national Managing Authority)

Discussions with the EIF/EIB may play a role at this stage, as well as with the Commission. At this and later stages, wider political concerns (political support for FIs within the region/MS) have an influencing role.

"The EIF played a crucial role in deciding to set up FIs." (national Managing Authority)

"Recommendations about possible financial proportions for each TO were provided in the EU Structural Funds evaluations carried out in the period 2007–2013. So it was relied on the recommendations of these evaluations as well." (national Managing Authority)

2. ***During the OP drafting and approval process*** – the OP must make reference to FIs if there are plans to use them, although this can take the form of only very general information (a 'placeholder'). The Commission plays a strong role at this stage, during the negotiation process.

"Very general information was in the programme document but it was not very concrete. The main reason was not to "close the door" to potential FIs implementation." (national Managing Authority)

"Negotiations with the Commission affected planners' thinking, pressure from the Commission was apparent though not absolute." (national Managing Authority)

Previous use of FIs is a strong indicator of future use, at least, where that previous experience was positive.

"It was a natural continuation of past experience and the use of FI was proposed while negotiating and drafting OP." (national Managing Authority)

"The approach therefore was a natural continuation of the past and the concepts has been present in the strategic thinking process from the commencement of the programming exercise." (national Managing Authority)

"It was a natural decision" (regional Managing Authority)

"The decision to make use of FIs was logical….the positive experiences of the 2007-2013 programming period have been a decisive factor to choose FIs for the 2014-2020 programming period" (regional Managing Authority)

In the OPs, the indicative amount allocated to FIs tends to be influenced by **the total budget available, the OP priorities, expected absorption capacity, and other resources** available, including amount of revolved funding. The OP figure must be indicative only, as funds cannot be allocated to FIs until an ex ante assessment has taken place.

"The level of funding allocated to FIs was decided based on past experience, expected absorption capacity, recommendation of the EC." (national Managing Authority)

"The financial allocation to the 2014-2020 FIs was determined by the amount of revolving resources obtained from the 2007-2013 programming period." (regional Managing Authority)

"The level of resources allocated to FIs has been determined by the level of resources previously devoted to grants. There has been a transition between types of support but the budget has not been substantially altered." (regional Managing Authority)

"Mainly related to experience from the past but also based on the level of co-financing that is available." (regional Managing Authority)

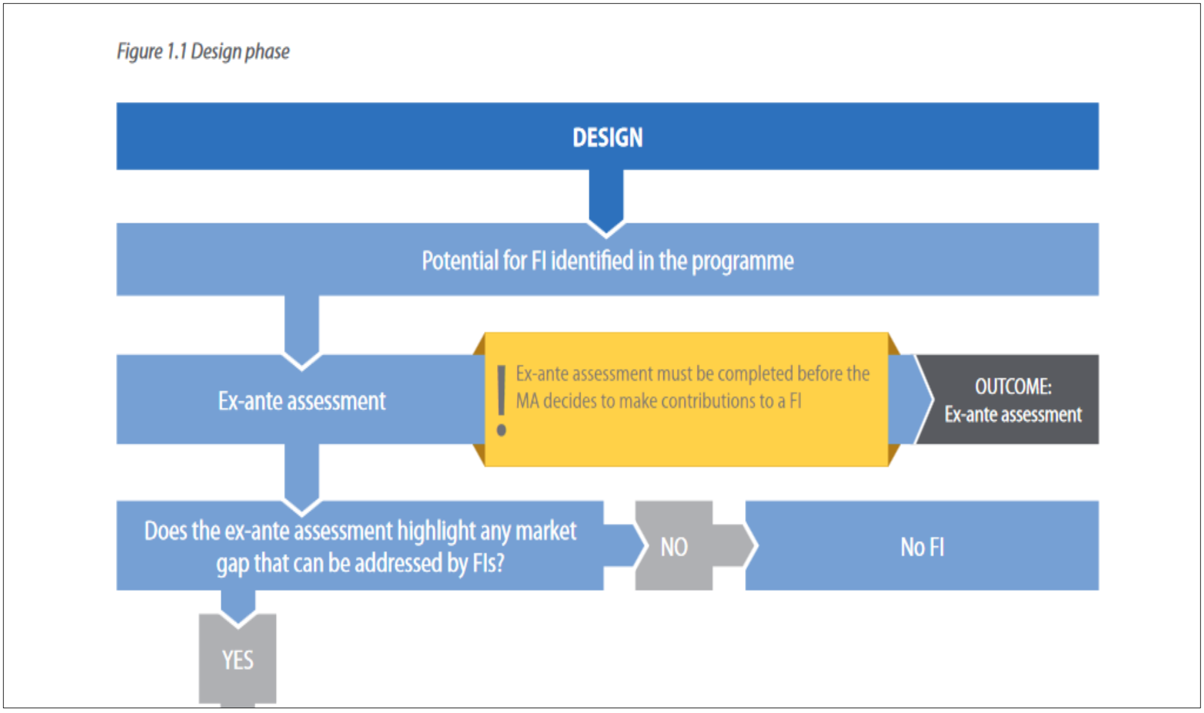
3. *The ex ante evaluation of OP* may confirm the approach taken in the OP or challenge it. This was not mentioned by MAs as having been a strong influencing factor on the decision whether or not to use FIs.

4. *The decision to procure an ex ante assessment*. A **wide range of approaches** have been taken to this process among Member States (a more detailed analysis is provided in the First Interim Report). They have variously been conducted at OP level (regional and national), Priority Axis level, Fund level, for individual FIs (mostly in Germany), or have reviewed individual Investment Areas, spanning across ESI Funds and national and regional OPs.

5. *The recommendations of the ex ante assessment* – if an ex ante assessment goes ahead, the MA may decide to accept its recommendations in full, to adapt them, or not to adopt them at all. The ex ante assessment's recommendations may or may not be consistent with proposals made in the OP, and **may require a change in plans** – in the amount allocated, in the type of FI proposed and in the TO(s) being addressed.

> "The ex ante is still in progress and only with its finalisation the level of funding allocated to FIs will be determined." (regional Managing Authority)
>
> "Definitely yes, the ex ante assessment was important resource for discussion on future FI implementation. Other factors: previous experience, recommendation of the EC." (national Managing Authority)
>
> "discussions were based on past absorption capacity, findings of ex ante assessment and expected engagement of other resources, the discussions with the EC influenced the level of funding [for a specific measure]."(national Managing Authority)
>
> "The OP is fully in line with the ex ante assessment's findings. TOs, types of financial products and allocations have remained unaltered." (regional Managing Authority)
>
> "There are some thematic differences (e.g. the ex ante assessment recommended to support renovation and construction (within energetic savings) via FIs, the MA decided to focus only at renovations) or differences linked to forms of FIs – equity recommended but not implemented (considered as a too strong for applicants who are not sufficiently familiar with the FIs within 2014-2020 programme period)." (national Managing Authority)
>
> "There have been adjustments to what was originally planned in the OP. The OP was intentionally drafted in a quite generic manner to leave room for adjustments." (national Managing Authority)
>
> "The implementation of FIs is not fully consistent with the OP. Some existing ideas were discarded and some new were added after the OP was drafted." (regional Managing Authority)
>
> "The implementation of FI is consistent with recommendations of the ex–ante assessment. For example, in case of support for SME, all recommendations provided in the ex–ante assessment were implemented. There were defined the selection of type of FI, the financial allocations for implementing FI selected, establishment of fund of funds." (national Managing Authority)
>
> "The only change was diminishing some of the allocation previously planned for [a specific priority] - after the assessment we decided that there will not be enough demand for financial products in this sphere." (regional Managing Authority)

Figure 4.19: Decision process - using FIs in the OP



Source: European Commission and EIB (2015) Developing an action plan Design, set-up, implementation and winding-up of financial instruments, fi-compass https://www.fi-compass.eu/sites/default/files/publications/ESIF-factsheet-developing-action-plan.pdf

4.10. Does the current legislative framework facilitate or hinder the uptake of FIs?

The 2014-20 Regulations underpinning the use of FIs are a step change from those applicable in 2007-13, partly in response to Member State concern at the absence of detail and lack of clarity in those rules in the previous planning period.

The ***general perception*** of Managing Authorities on the new legislative framework is rather mixed, though it is fair to say that it is generally found to be challenging. Some respondents were *positive* on the new Regulations:

> "Very helpful and better than 2007-13" (financial intermediary interview)

> "The 2014-2020 Regulations are clearly a step forward compared to the 2007-2013 Regulations. In that sense, they are more helpful." (Managing Authority interview)

> "The 2014-2020 Regulations are assessed as sufficient, including of the level detail." (Managing Authority interview)

> "The 2014-2020 Regulations are definitely better and more detailed with respect to FIs and this is appreciated." (Managing Authority interview)

However, the view that the Regulations *could be improved* was more widespread. A key area of concern is the uncertainty associated with the scope for interpretation in the Regulations:

> "2014-20 Regulations [are] too onerous, detailed, bureaucratic, complex – more than in the 2007-13 period" (financial intermediary interview)

> "Too detailed and especially not always clear interpretation (and very limited possibilities how to check the correctness of the interpretation due to lack of follow-up communication with the EC)." (Managing Authority interview)

> "The 2014-2020 Regulations are extraordinarily complex and do not offer much flexibility. In particular, there are different perceptions in the private and public sectors. When FIs involve the private sector, the Regulations are not appropriate. For instance, there is too much unnecessary bureaucracy and problems arise from the rules on eligibility. These obstacles have resulted in [financing] FIs with own funds (the revolving from past programmes), as opposed to ERDF resources." (Managing Authority interview)

> "FI management is very complex. There is legal uncertainty in control audits that could affect the execution. … The granting and monitoring of an FI should not have many more controls than those who have a loan from a bank. The management and control of an FI should encourage their use, rather than discourage it." (Managing Authority survey, user).

> "The 2014-2020 Regulations have been helpful to some extent. However, when it comes to complex legal questions there is often room for interpretation." (Managing Authority interview)

> "Although there has been progress in addressing the legal uncertainty experienced in the previous period, the volume of regulations is a general concern. The complexity of the regulations, difficulties of overseeing the regulatory landscape are great problems." (Managing Authority interview)

> "The Regulations set the MA off in one direction on the selection process, but the selection guidance has just been approved…. [our] interpretation of the Regulations implied the MA could use calls but this was negated by the guidance when it emerged." (Managing Authority interview)

Another major concern is with ***timing*****.** This relates both to the Regulations themselves and to guidance issues in support of them:

> "Regulations are considered as useful, only they were issued late." (Managing Authority interview)

> "… have found piecemeal way they came out difficult, the same for the guidance that then interpreted the Regulations." (Managing Authority interview)

> "The EC frequently responds late, sometimes not at all and concurrently the EC pushes the member states to implement the FI as soon as possible." (Managing Authority interview)

> "… guidance documents appear late, too late. When we started our FIs ex-ante analysis some of them were not present…. now we have to change / revise the analysis. There is an important need for better coordination of these processes on the EU level." (Managing Authority interview)

> "Commission's procedures are too long and complicated. For example, the guidance for selection of intermediaries implementing financial instruments are approved just in the second part of 2016. There is also 2 years timing gap between the approval of the Commission's Regulations and issuing more detailed explanations, which create a lot of discussions, additional questions, delays and dissatisfaction …." (Managing Authority interview)

The introduction of obligatory ***ex ante assessment*** to underpin the use of financial instruments was generally viewed very positively.

> "obligatory ex ante assessment is considered useful" (Managing Authority interview)

> "Obligatory ex-ante assessment is considered as a very useful tool, it shows the fundamental perspective how to deal with FIs." (Managing Authority interview)

> "Ex ante assessment was considered as very useful … would recommend it for grants." (Managing Authority interview)

However, some expressed concerns at the time involved and considered that the Commission should have a role in feeding back on the ex ante assessment:

> "ex ante assessment is not evaluated and approved by the Commission, which leaves a lot of questions open, i.e. related to mechanisms for implementing FIs. Feedback from the Commission on the ex ante assessment would be very useful."

> "the ex ante … should be instrumental in clarifying issues not resolved by the documents already provided but it is too time-consuming…the implementation is delayed and efficient management is hindered."

In addition, while the ex ante assessment was generally welcomed, some expressed concern at the level of detail required and questioned whether market needs could realistically be predicted on such a long term basis.

> "key challenges seem to be economic ones due to the fact that ex-ante assessment was carried out in 2014 based on data from 2012-13. Economic conditions… have changed substantially since then." (financial intermediary interview).

There are also mixed views on the rules concerning ***management costs and fees.*** Some considered these to be a constraint on policy design, while others were content at the new provisions:

> "…management costs and fees are not considered as a constraint" (Managing Authority interview)

> "The decrease of management costs and fees is understandable but finally very radical. The MA has to resolve covering of real costs with intermediary." (Managing Authority interview)

> "the current management fee and costs provisions require a very complex calculation method. The performance focus is welcome, however there are many dilemmas concerning their application. The previous model is perceived to have been simpler, more transparent and market-friendly, priced by market actor in line with market practices." (Managing Authority interview)

> "Management costs and fees: these are a constraint, but a necessary constraint. They don't give flexibility for certain types of fund to operate effectively but it is right to have set fees and costs. A little more flexibility in certain circumstances where it could be justified might be desirable." (Managing Authority interview)

> "In 2014-20 the fees and costs… have been limited to 1%. This means we can no longer cover our costs…. The administrative costs should be covered by repayments and gains. This was confirmed by the Commission in a long communication process but it is not clear if the later inspectors will accept the emails of the Commission… as a basis for their inspection (financial intermediary interview).

"Ridiculously low given the risk and liability assumed". (financial intermediary interview).

"As the costs of managing a FI is not uniform across the years, provisions of linear MC&F are damaging especially for in-house financial bodies. This creates financial reporting problems, whenever the payment of activities in a year is delayed to the following years(s). Technically it is incorrect to have active costs in a year which are reported/claimed ex post." (financial intermediary interview).

"Adequate… but perhaps not sufficiently flexible for lower scale FIs – many private sector fund managers may not be willing to engage in smaller funds due to the limitation on proportional remuneration. Minimum absolute amounts could help." (financial intermediary interview).

Another area that elicited comments from Managing Authorities concerns ***phased payments***, these provisions were new in 2014-20 and designed to counter the overcapitalisation of funds that had occurred in 2007-13, partly as a mechanism to postpone possible decommitment. Whilst generally accepted (or not commented to any large extent) some specific issues emerged:

"Phased payments – it is a good idea, however due to very hard conditions (the third applications for payment can only be submitted once 85% of the amounts have been spent) and even more national rules make it rather a constraint. More flexible system would be more beneficial." (Managing Authority interview)

"the provisions on phased payments are not realistic in the private sector since capital calls are made on a rolling basis usually." (Managing Authority interview)

"When the implementation of FI is very successful (because of high demand and a large quantity of projects), the threshold of 25 percent is too low, as there is a lack of funds … lack of resources also arises because of the limitation imposed by the Article 41 of CPR on the second and subsequent disbursements, which depends on the incurred eligible costs (by 60 and 85 percent). Periods of lack of funds basically show that the fund could operate more efficiently, but it is limited by Regulation." (Managing Authority interview)

Some detailed ***eligibility*** issues were also mentioned:

"some of the rules are not market based, e.g. those related to property. ERDF states that you cannot put more than 10% grant towards property. I can understand this for grants, BUT if you have a business which is planning to buy a property instead of renting and wants to use FIs, this should be different" (financial intermediary interview).

Last, the ***implementation options*** also attracted comment, with some respondents considering the EIB and EIF to be in privileged position in relation to domestic financial intermediaries, but others having a more positive view:

"The implementation options are not favourable for in-house financial bodies…in-house financial bodies are disadvantaged compared to private/other operators. Again, the EIB/EIF model is largely incentivized…. The EIB has less administrative burdens (monitoring and control) and the whole mandate seems to be less transparent." (financial intermediary interview).

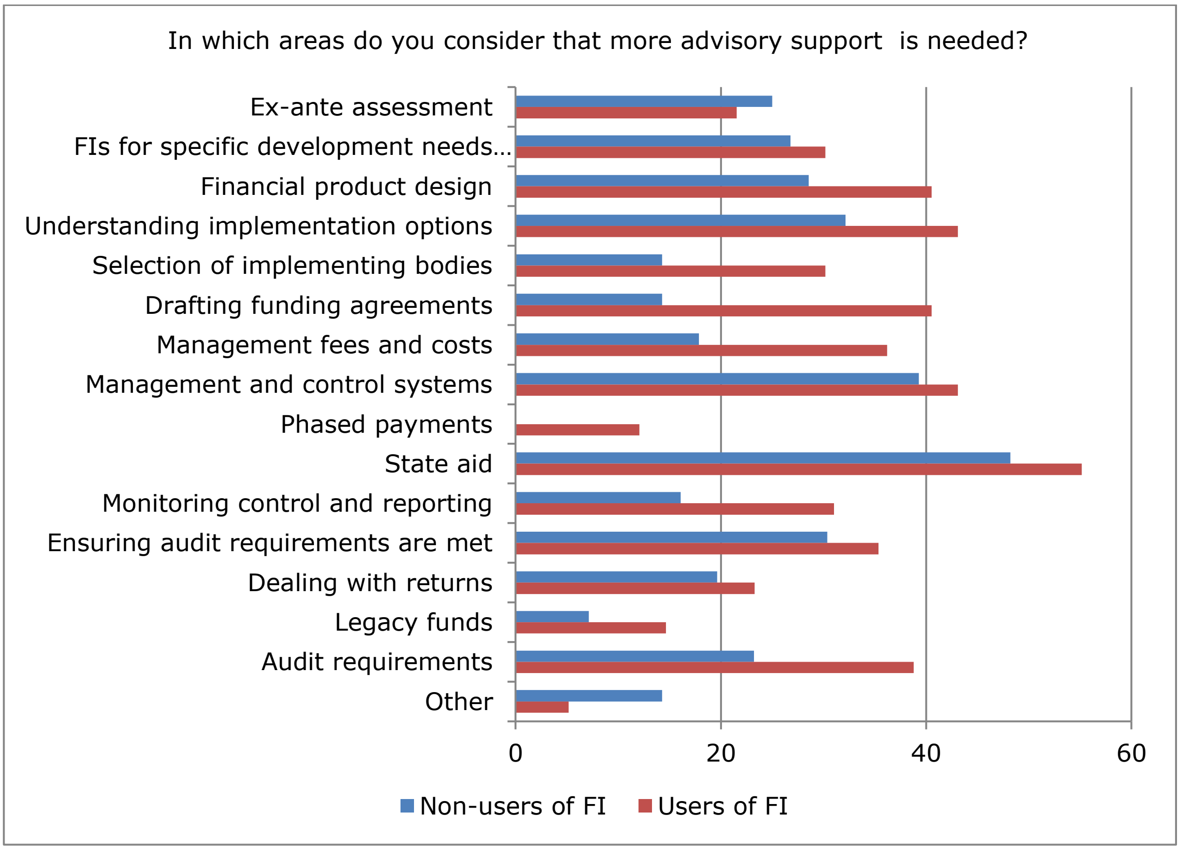
"Provisions on public procurement are inappropriate for the selection of implementing bodies/intermediaries…. One of the major obstacles of the implementation process… the aim of the selection is to choose the provider with the highest quality, not the cheapest offer. Requirements for the selection simply cannot be fully respected in the given legal framework" (financial intermediary interview).

"from our experience the selection process for intermediaries, from the EIF, is very transparent" (financial intermediary interview).

4.11. To what extent does the available guidance and advice address support needs?

The legislative framework for financial instruments in 2014-20 has been characterised by considerably increased emphasis on support, notably through *fi-compass*, and on written guidance issued by the Commission. Nevertheless, a significant number of Managing Authorities think that more guidance is needed in certain areas. The emphasis of these needs varies between those MAs using FIs and 'non-users', largely reflecting the extent of their experience with implementation (see Figure 4.20).

Figure 4.20: Advisory support needs among Managing Authorities



Source: EPRC online survey of Managing Authorities.

There were a number of other comments on advisory support from the survey, mainly from non-users identifying specific needs:

"Best practice of other countries in detail" (Managing Authority, non-user).

"Experience from ETC programmes (Interreg) that have used FIs would be interesting to understand if they would be relevant for us. Currently the understanding of FIs is very limited in ETC and thus it is difficult to assess the potential benefit." (Managing Authority, non-user).

"Financial instruments in cross-border (Interreg) context are again much more difficult, as regulations of several countries apply" (Managing Authority, non-user).

In addition, some FI users commented on possible other advice, focussing on the need for guidance to be tailored to national circumstances and dealing with specific needs:

> "…masses of written guidance will not be as useful as a unit which deals with reality on the ground - someone we can speak to about making the best use of the funds rather than an over-reliance on rules would be fantastic. i.e. helping us work within the rules not just regurgitating them at us." (Managing Authority survey, user)

> "fi-compass could include more examples of good practices on how other regions / countries deal with the implementation of FI. On fi-compass they could also publish EC documents, which are under development, so that potential users had access to them during their development." (Managing Authority survey, user).

> "The guidelines established at the European Commission do not translate into legal solutions at the national level. We do not see any simplification of the implementation of FIs…. FI organization is more complicated than it was in the 2007-2013 financial perspective." (Managing Authority survey, user).

> "The newly established Wikipedia [Regiowiki] is better but some links are not always visible or they are not linked. Nevertheless, the Wikipedia represents a step in the right direction." (Managing Authority interview).

In addition, some expressed the view that the issue was not with the *guidance*, but with the underlying *regulations*.

> "The problem of the financial perspective 2014-2020 in the field of financial instruments is not strictly the lack of counselling support, but over-regulation system." (Managing Authority survey, user).

> "If Managing Authorities need advice, it is because the system is too complex. It would be better to simplify the system than to develop advice."(Managing Authority survey, non-user).

These perceptions are line with the wider views gathered at interview which suggest ***three main issues associated with guidance: timing, tailoring and status.***

Regarding, ***timing,*** there has often been a significant gap between the regulation being issued and guidance being available.

> "The only problem mentioned was timing. It was issued late." (Managing Authority interview)

> "…it takes too long to issue official Guidelines" (Managing Authority interview)

> "The timing of the selection guidance was extremely late, the final version issued in mid-summer 2016; meanwhile MA completed a public procurement process in order to be able to commence lending. Also, … there was no real opportunity to influence the content." (Managing Authority interview)

> "The main problem is that the guidelines are drawn up late. They are approved when the financial instruments are already being implemented." (Managing Authority interview)

> "Written guidance provided by the Commission could be closer to Regulations timewise." (Managing Authority interview)

> "Timewise the ex ante guidelines were delayed and received after the ex-ante assessment was already prepared and for this reason it had to be revised." (Managing Authority interview)

> "Guidance was generally good but late. This can't be helped because of the lengthy negotiation period. Also for the 2014-20 period there seem to have been an unusual high amount of implementing and delegated acts which delayed things considerably." (Managing Authority interview)

> "Unhelpful when it comes out at a different time from the Regulations and where it muddies the water. Guidance should be available at the same time as the Regulations." (Managing Authority interview)

The second, main issue raised is ***tailoring*.** Many MAs consider the guidance to be too general for their needs, and often too theoretical or lacking in practical examples and would like more, and more effective, direct contact with the Commission on their specific needs.

Box 4.5: Managing Authority experience with guidance and communication

"The guidance did answer the key questions but …the system is very complicated, interpretation of some points is not clear and the MA has not a good experience with follow-up communication with the EC ……e.g. no reactions on comments, no reflection of comments and no explanation why they were / were not reflected. The written guidance was issued late."

Source: Managing Authority interview.

Specifically on the ***SMEI***, one Managing Authority noted:

> "There is almost no written guidance about the SME Initiative" (Managing Authority interview).

> "One of the problems with the SMEI is that is doesn't leave behind any expertise or capacity with the national authorities" (Managing Authority interview).

Box 4.6: Participation in the SME Initiative

One of the innovations introduced by the CPR in 2014-20 for ESIF FIs is the possibility for Managing Authorities to make a contribution to a financial instrument set up at Union level. .The SME Initiative is an example for a financial instrument set up at Union level implemented by the EIB Group which aims to stimulate SME financing by providing partial risk cover for the SME loan portfolios of the participating originating financial institutions. Alongside ESIF resources contributed by Member States, the SME Initiative is supported through COSME and/or Horizon 2020 resources at EU level, as well as EIB Group risk cover.

The initiative offers two products: an uncapped portfolio guarantee instrument and a securitisation instrument and operates via financial intermediaries selected by the EIF in the Member State concerned via an open call for expression of interest. The financial intermediaries undertake to provide SME loans, leasing and/or guarantees at favourable terms (for example, reduced interest rates and collateral requirements for the final recipients).

SME Initiative OPs have so far been approved by the Commission for Spain, Malta, Bulgaria, Italy, Finland and Romania. The uncapped portfolio guarantee instrument is being used in BG, ES, FI, MT and RO, while the securitisation option has been chosen in IT. Challenges so far identified stem from the newness of the tool and the learning curve associated with an unfamiliar initiative. The lack of clarity on the MA's role and the lack of written guidance were raised as issues.

Source: EPRC case study research – see Annex 1.

More generally:

> "The guides published by the Commission were of help to some extent. However, the guides are drafted in view of 28 Member States and they sometimes are not

applicable to our OP with its own particularities. A way to improve the guides could be to add more examples." (Managing Authority interview)

"The written guidance is helpful only to a limited extent. For some of the more complex issues the information provided therein is too basic." (Managing Authority interview)

"The written guidance was used to some extent to get acquainted with FIs but it does not resolve complex issues which arise in practice when implementing FIs." (Managing Authority interview)

"The written guidance provided by the European Commission could be improved by incorporating practical examples and less theory." (Managing Authority interview)

"Guidelines are perceived as useful and thorough. Examples made can sometimes be useful, but oftentimes they don't fit the specific context of this OP." (Managing Authority interview)

"It should also be possible to have in place fast consultation mechanism with the Commission personnel responsible for FIs." (Managing Authority interview)

The third issue is the ***status*** of the guidance, the impact this can have on audit, and the perception that the Commission sometimes applies stricter rules in the guidance than is implied by the regulations themselves.

"In theory, the application of guidance is not mandatory, nevertheless experience has shown it being a reference document for EC auditors. Therefore, any draft needs to scrutinised by the MA for potential audit risks." (Managing Authority interview)

"There are cases where the guidelines are more restrictive than Regulations. They impose restrictive conditions which were not specified in the Regulations." (Managing Authority interview)

"Without guidance the regulatory risks are too high to decide on implementation of any financial instruments. And more, the guidance (helps of course) but still open room for various interpretations … a system in which a regulation needs guidance (of unknown legal power) is somehow, say, incorrect." (Managing Authority interview)

"…the guidelines should be binding and - if changed - should not work to the past (be retroactive) - this is a basic condition that must be secured." (Managing Authority interview)

"We do the things based on our best understanding, we do not have any security that we do things correctly." (interview, Financial intermediary)

"Written guidance is issued rather later. Although the EC guidelines are no obligatory, the auditors seek full conformance with them and some of the measures were already implemented due to the time constraints." (Managing Authority interview).

"60% clarified 40% grey area. Needs to be watertight. Written guidance opened up quite some discussion. Does not help when it comes to audit." (Managing Authority interview)

4.12. What changes to the legislative environment would assist FI implementation or encourage FIs where they are not used?

In considering what changes to the legislative context might facilitate the use or take-up of FIs, one specific topic - State aid regulation - was cited by a number of Managing Authorities, and three broad themes emerged from the interview programme. These are: communication with the Commission; training, information and advice; and simplification.

The concerns about ***State aid*** expressed in interviews are consistent with the outcome of the Managing Authority online survey in which State aid emerged as the single most important area about which more support was needed (see Figure 4.20).

> "State aid was only applied in the form of *de minimis* in the previous programming period, experience of other State aid provisions has been missing." (Managing Authority interview)

> "Simplification in relation to State aid regulations is needed. EC State aid regulations are creating a lot of problems for both intermediaries and beneficiaries." (Managing Authority interview)

> "Compatibility with State aid is crucial. Colleagues in other departments are discouraged by the complexity of FI, in particular with reference to State aid." (Managing Authority interview)

> "The Commission should expand the options for off-the shelf instruments (FI models), compatible with State aid. "(Managing Authority interview)

> "Definitions and regulations are not uniformly defined under the different funds. For example in relation to subsidies and de minimis" (Managing Authority interview)

Communication between the Commission and Managing Authorities is evidently a source of frustration to MAs, and several note that improving this would facilitate the use of FIs in future:

> "Possibility of direct consultations with the European Commission (some issues were not sufficiently clear, especially at the moment of the process of setting up of the system)." (Managing Authority interview)

> "Better communication with the EC, modification of some conditions (e.g. those of repayable assistance)." (Managing Authority interview)

> "Better communication with the EC, more practical information, feedback for specific issues." (Managing Authority interview)

> "Better consultation mechanism, if detailed interpretations are needed, without "notes" underlying that no one is responsible for what was settled in this consultation mode." (Managing Authority interview)

Information, training and exchange of best practice were also cited as measures that would facilitate the use of FIs in future, or encourage their use, and the following points were among those that emerged from interviews with Managing Authorities:

> "The EIB-EC's *fi-compass* platform was evaluated positively and further workshops should be organised [here]. Training should be tailored to [our country]." (Managing Authority interview)

> "Further development of *fi-compass*. However, it must be noted that there is a conflict of interests, since the EIB Group provides information and at the same time has an interest in product marketing." (Managing Authority interview)

> "Further development of the *fi-compass* platform would be evaluated positively, to strengthen the support for Managing Authorities." (Managing Authority interview)

> "Exchange of best practices of successfully implemented FI in other Member States with practical examples and hints how to avoid most common mistakes." (Managing Authority interview)

> "The establishment of an efficient Advisory Centre would be useful as well as the dissemination of the good practice." (Managing Authority interview)

> "Access to a well-organized data base of examples, how FIs may be adopted in various policy areas." (Managing Authority interview)

> "Institutions still do not know how to use [financial instruments] properly (there are not many experts on this topic in public administration). This requires further support (trainings, examples on the use, support in implementation, better promotion)." (Managing Authority interview)

Also, awareness raising about the availability of FIs was mentioned:

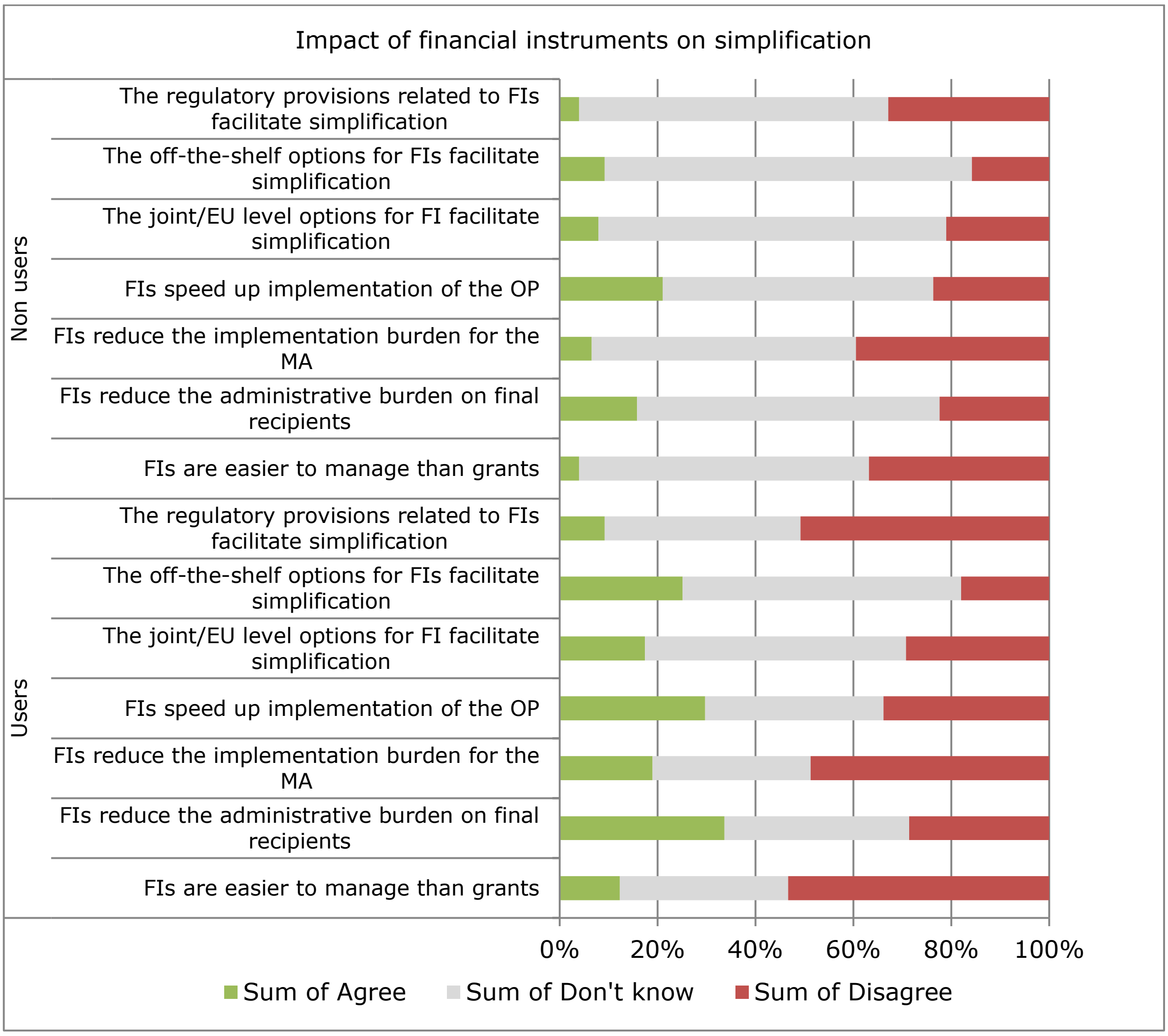
> "…more awareness should be raised on these products vis-à-vis banks and firms. For instance, I am not sure how many commercial banks know that there are several products for municipalities or for energy-efficiency that can now be accessed. This awareness should be increased through marketing campaigns as well as through political messages from national governments and central banks" (Managing Authority interview)

Specifically regarding EMFF one Managing Authority noted that:

> "A national event tailored to the fisheries sector would be extremely welcome, as would an off-the-shelf-instrument tailored specifically to the needs of the fisheries sector."

Simplification is currently high among Commission priorities and echoes the desire of many Managing Authorities to find easier ways of implementing policy. However, the scope for financial instruments to contribute to the simplification agenda appears rather limited at present. Most Managing Authorities did not have a view on the role that FIs could play in simplification in the current period, but among those that do, the perception is that FIs have a negative impact, as Figure 4.21 shows. Moreover, on some issues, the perceptions of MAs are *more* negative among those who currently use or plan to use FIs than among non-users.

Figure 4.21: Perceptions of the impact of FIs on simplification (all Funds)



Source: EPRC Managing Authority survey.

Notwithstanding current views, a wide range of general and specific simplification issues were identified during the interview programme. Some related to specific aspect of FIs, such as monitoring, possible off-the-shelf instruments, selection of intermediaries and eligibility:

> “the verification/monitoring procedures are quite cumbersome and should be simplified.” (Managing Authority interview)

> “the off-the-shelf instruments should be opened up to more types of activity supported.” (Managing Authority interview)

> “a wider range of off-the-shelf instruments could facilitate making use of more FIs in areas where they are currently not being used.” (Managing Authority interview)

> “Selection of financial intermediaries: it would be useful to implement the selection procedures in accordance with good practice [of the] EIF and to run an open and transparent bidding process. Now public procurement rules are applied. The bidding process would be better because FI should be flexible. Besides, it is difficult to determine the right (with unlimited competition) selection criteria. It has to be noted that public procurement procedures limit the financial feasibility of the measures.” (Managing Authority interview)

"It is important to provide opportunities for supporting large enterprises (limitations of ERDF regulation)." (Managing Authority interview)

"The programme's end time differed from the instrument's one. The fund life cycle was expanding until after 2020. One investor could not therefore participate to the full cycle, which makes no financial sense… It would be goo that once paid to a fund (but not invested) OP money be repaid in a more flexible manner: not at the end of the programme period but at the end of the instrument cycle" (financial intermediary interview)

Other issues were more general, such as the need for ***better coordination,*** shorter texts and more proportionality:

"European Institutions should be more swift in their coordination tasks. Some procedures are too time-consuming." (Managing Authority interview)

"Reducing administrative burden for FIs is crucial, too. It is repayable, actual aid accounts for a small fraction of grant assistance while the volume of administrative requirements for these two types of support forms have become very similar." (Managing Authority interview)

"In order to guarantee the efficiency of the financial instruments, it should be relied on financial institutions practice and refuse accumulating and storing excess documents, which increase the administrative burden." (Managing Authority interview)

"Regulation should be more concise." (Managing Authority interview)

"specific needs of the final beneficiaries and reducing of the administrative burden have to be taken into account." (Managing Authority interview)

"Rationalization of legal framework" (Managing Authority interview)

"A shortcoming is in the excessive fragmentation in the regulations. Different rules and procedures spread out in several implementing regulations and guidelines. This should have been rationalized." (Managing Authority interview)

"More stable "legal" environment on the level of guidelines concerning using FIs." (Managing Authority interview)

"The 2014-2020 Regulations have room for improvement. Simplification is needed in terms of compatibility between FIs and grants and reporting requirements… it is not reasonable to impose the same reporting requirements to operations of different size." (Managing Authority interview)

"Various caps and targets. Understand where this is coming from. We do our best to achieve them, but subject to market. Sometimes unfair that penalties apply when we have already said that we believe that market is very small. Lots of funds didn't meet targets last time, so now targets tighter, better to stagger payments so not overexposed. However, if it becomes ridiculous - intermediaries will withdraw. Financial intermediaries are not making money from these schemes; it's because we may make some new business from this. On a CBA the bank struggles to justify its involvement - it's only because of the possibility of generating new business, not because of the income generated. All recommendations to tighten up follow the CoA report. Be cautious or you will kill the involvement of the financial intermediaries!" (Interview financial intermediary).

Some had sector-related concerns regarding uptake:

> "Specifically for transport, the FIs could be excluded from the calculation of the budget deficit".

Last, and perhaps controversially, ***differentiated rules*** to reflect experience were suggested by one Managing Authority interviewee.

> "For some lesser developed countries the detailed regulations are perhaps helpful and they provide clarity and certainty. However, they do not leave enough room to tailor the FIs to the needs in the Member State. Also [our] politicians are not used to this high level of rules and it can be quite difficult to explain to them why they can or cannot implement a certain FI. Perhaps there should a pre-exam which would allow those OPs that have a lot of experience to implement FIs using less stringent regulations?" (Managing Authority interview).

5. THE RELATIONSHIP BETWEEN ERDF, COHESION FUND, ESF AND EMFF FIS AND EU LEVEL INSTRUMENTS AND EFSI

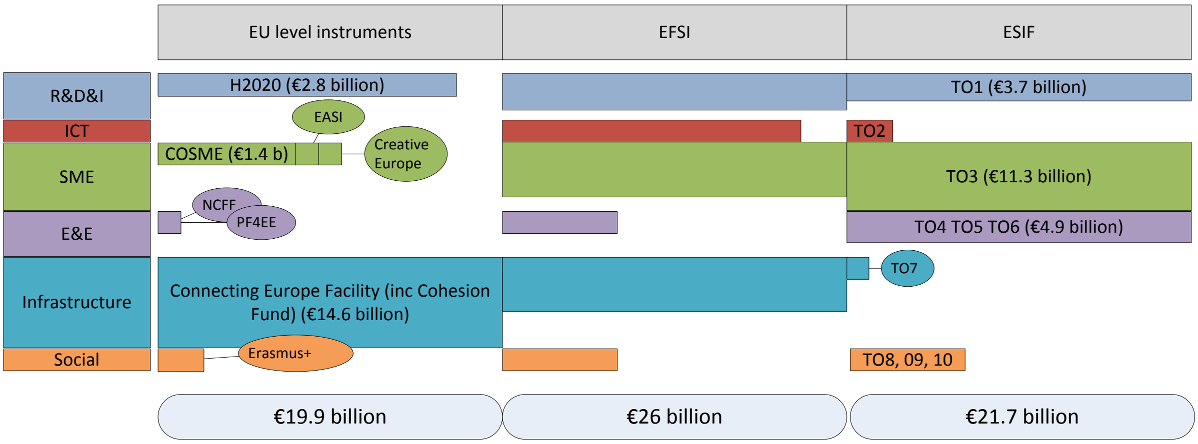
Key findings

- The funding landscape is complex and becoming increasingly so. Managing Authorities generally believe ESIF FIs and domestic sources of funding (public and private) complement one another.
- MAs now have a wider range of options for implementing FIs – contributing to a financial instrument set up at Union level such as SMEI, seeking synergies with COSME, InnovFin, and EaSI, as well as the newer EFSI.
- The relationship between ESI Fund FIs and other EU instruments of various kinds is not well understood.
- MAs where an ex ante has been completed are better able to form an opinion about the relationships between ESIF FIs and other instruments; these MAs are more likely to perceive there to be competition between ESIF FIs and other instruments than those MAs where no ex ante has been done.
- There are concerns about the relationship between ESIF FIs and other EU sources of finance, especially concerning the competitiveness of the former.
- There are overlaps between ESIF and EFSI and while some think there are opportunities for synergies, most consider these to be highly challenging.

ESI Funds are part of a complex landscape of funding mechanisms, including from private and public, domestic and EU-funded sources and at regional, national and EU levels. MAs can contribute ESIF resources to a financial instrument set up at Union level such as the SME Initiative, and other EU-level instruments (often managed by the EIB Group).

The scale of funding under the various measures is often difficult to determine, partly due to overlaps between initiatives, but can also be quite fragmented, as illustrated in Figure 5.1.

Figure 5.1: Estimating the scale of EU FIs by source and objective



Notes: The boxes representing budget commitments are broadly to scale. In the case of EFSI, the breakdown of commitments as at November 2016 has been used as a proxy to disaggregate the commitment by objective for illustrative purposes, though clearly the past may not be a guide to the future.
Source: EPRC calculations based on Regulations underpinning the various initiatives and OP budget commitments for ESIF.

Figure 5.1 also illustrates that there is considerable overlap between the high level objectives of spend; moreover, although the sources are presented as distinct, in practice there is scope for overlap here too.

Indeed, the CPR makes specific reference to the possibility of contributing (ERDF and EAFRD) resources to the SME initiative. This enables MAs to contribute resources to FIs set up at EU level. So far, uptake of the initiative has been fairly limited; only Bulgaria, Finland, Italy, Malta, Spain and Romania have signed up to it. Part of the explanation for limited uptake may be contextual changes: the scheme was introduced to address liquidity problems in banks but these have been less severe than expected.

There is also a wider set of centrally managed EU-level FIs with which there are potentially important synergies with Cohesion policy activities, including COSME, which aims to improve access to finance for SMEs through loan guarantees and equity; InnovFin, the Horizon 2020 equity sharing and risk sharing instruments for innovative SMEs, and the Connecting Europe Facility, which provides finance for energy, transport and digital projects. These instruments have a long history and have been operating in various forms over several programming periods. The framework to facilitate MAs making contributions to EU-level FIs was introduced in the Financial Regulation and CPR for the 2014-20 period.

Another development at EU level is the introduction of the European Fund for Strategic Investments (EFSI), which was set up by the European Commission and the European Investment Bank as the cornerstone of the new Investment Plan for Europe. The Commission published guidance on ensuring coordination, synergies and complementarity between the two sources of funds in April 2016.[160] Alongside EFSI and financial instruments set up at Union level (including the SME Initiative), the EIB Group manages an extensive lending programme to support cohesion objectives; this includes direct loans, framework loans, intermediated loans and global loans.

In practice, however, the Managing Authority survey suggests that somewhat limited use is being made of the opportunity to contribute to these sources.

Box 5.1: ESIF FIs Combined with EFSI

There is potential scope for synergies or complementarities between EFSI and ESIF FIs, and there are several examples where this is being pursued:

EstFund in Estonia involves creation of a fund of funds (FoF) with a budget of €60 million: €48 million from ERDF and €12 million from the EIF's co-investment (under EFSI), as well as €35.2 million expected from private investors. The ESIF contribution includes returned funds from 2007-13. The FIs under the FoF will provide equity to final recipients, and include a Venture Capital Fund (€30 million), an Expansion Capital Fund (€15 million), and a Business Angel Co-Investment Fund (€15 million). EstFund will operate as a cross-border instrument; ESIF funds will be invested in Estonian SMEs and some private investor contributions can be invested outside Estonia. The EIF manages the FoF, fund managers for the FIs are currently being sought.

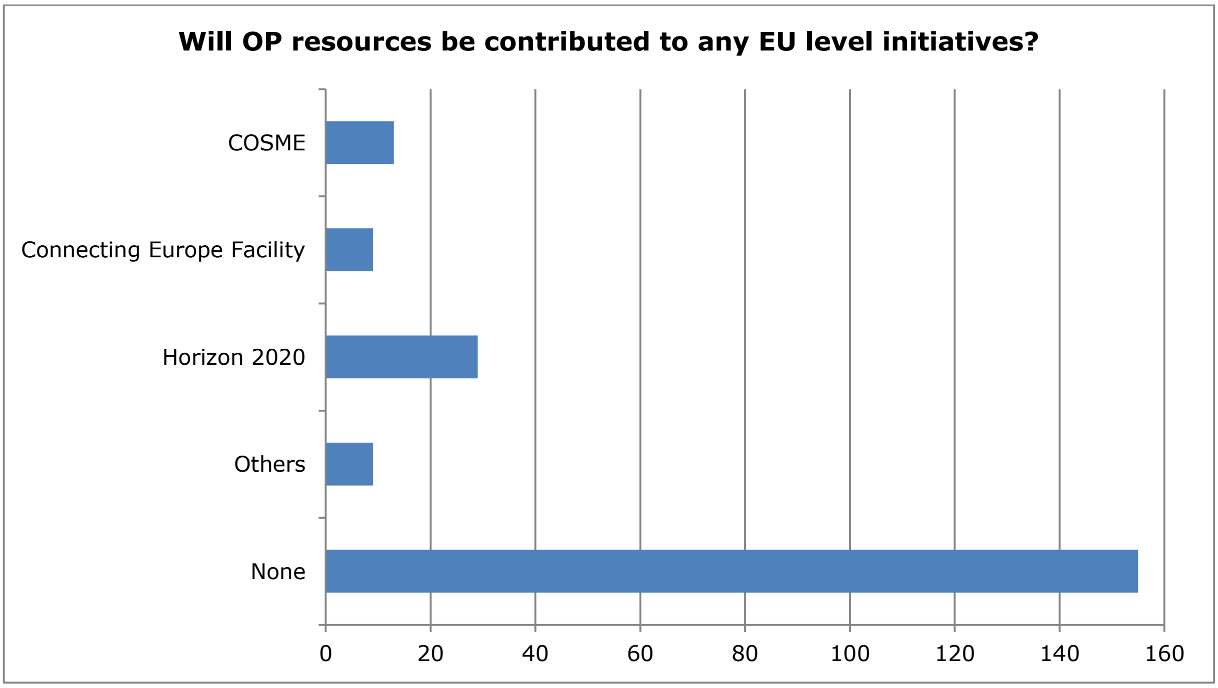
CAP 3ème Révolution Industrielle (TRI) launched by Région Les Hauts de France (Nord-pas-de-Calais/Picardie) will assist business-led investments in 'low carbon economy' projects. The total budget of up to €37.5 million is made up of €15 million from ERDF (€12.5 million as an FI and €2.5 million as a grant from TA), €5 million from Crédit Agricole Nord de France (commercial bank/private investor), and an EIB loan of up to €20 million, backed by an EFSI guarantee. The TA element will be used to fund technical, environmental or economic studies, either helping project promoters implement their projects or providing independent performance evaluation.

[160] European Commission (2016) European Structural and Investment Funds and European Fund for Strategic Investments complementarities, Ensuring coordination, synergies and complementarity
http://ec.europa.eu/regional_policy/sources/thefunds/fin_inst/pdf/efsi_esif_compl_en.pdf

The Swedish Venture Initiative is an SEK 582 million fund of funds initiative launched in April 2016 to support access to equity capital for Swedish early-stage high-growth enterprises. The Swedish Venture Initiative will invest in several early stage venture capital funds which will then invest primarily in Swedish enterprises. The Funding Agreement was signed with the EIF in April 2016, EIF are now looking for three funds managers, to be selected by an open call for expression of interest. The selected fund managers will receive a 'cornerstone investment' into their fund from the combined resources of the Swedish Venture Initiative and co-investment by the EIF.

Source: EPRC case study research – see Annex 1.

Figure 5.2: OP contributions to EU-level initiatives

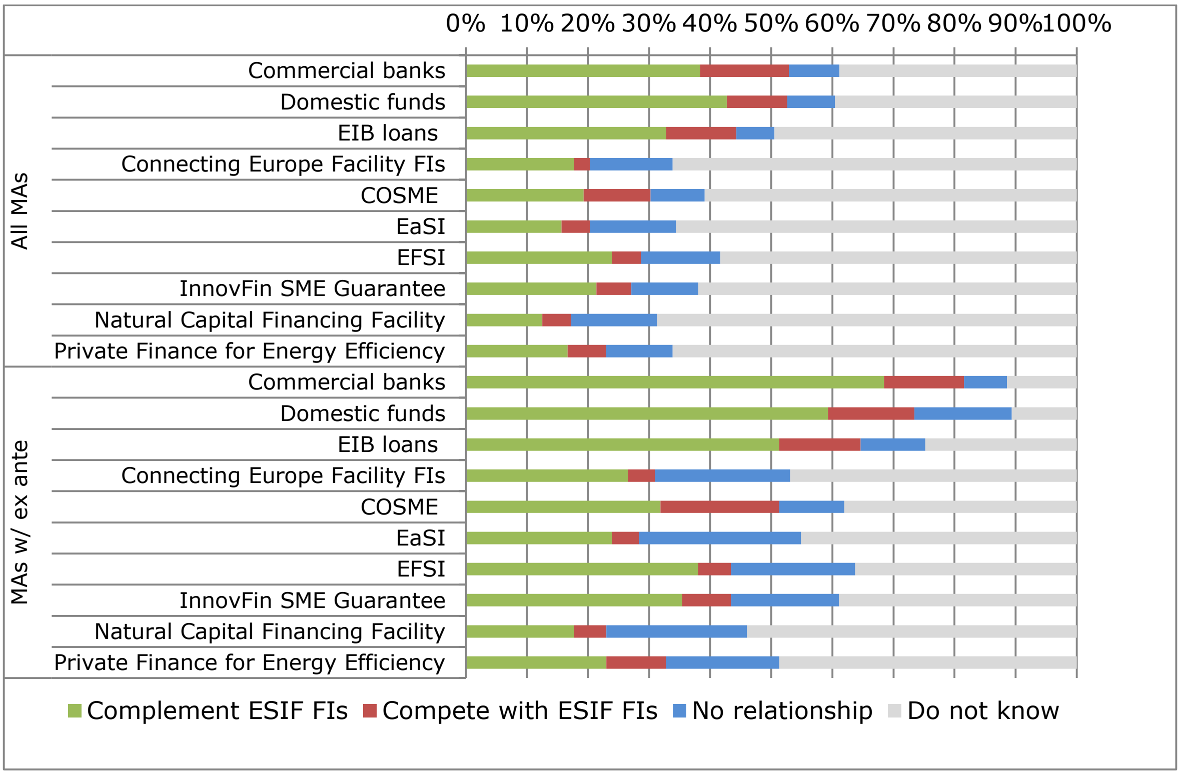


Note: From 194 respondents to this question, 155 did not plan to contribute to any EU level initiative. The 'others' mentioned were: SME Initiative, LIFE+ and plans to combine ESIF/EFSI funds

5.1. What is the relationship between ESI Fund FIs and domestic sources of finance?

ESI Funds contribute to a mosaic of funding sources at national, regional and local levels, and from the public and private sectors. However the relationship between ESI Fund FIs and domestic funding sources is not fully understood by Managing Authorities. Figure 5.3 suggests that around 40 percent of all Managing Authorities are unable to comment on the extent to which commercial and or domestic sources compete with ESI Fund resources. However, these overall perceptions are skewed by survey respondents from Managing Authorities which do not plan to use FIs, which were less likely to have an opinion on other instruments. Figure 5.3 distinguishes between all Managing Authorities, and those where an ex ante assessment has been completed. As would be expected, the latter are significantly better placed to express a view, although this varies by instrument.

Figure 5.3: Relationship between ESI Fund FIs and other instruments

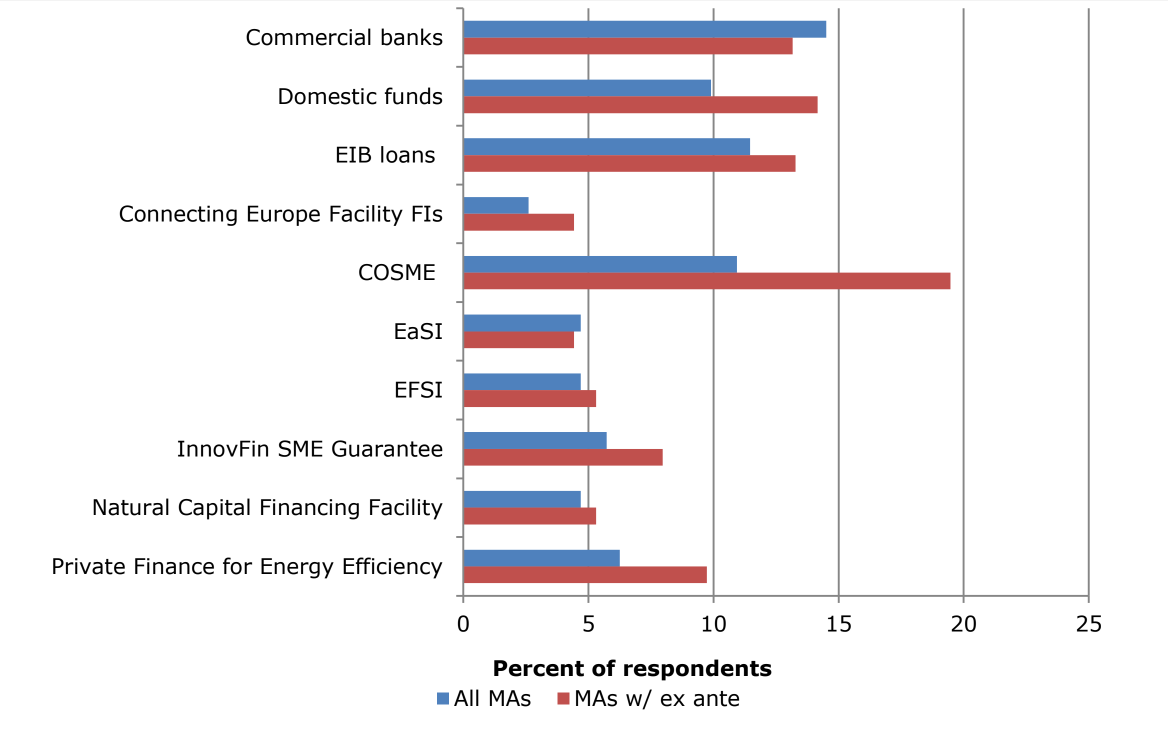


Notes: Managing Authorities, all funds, distinguishing those that have undertaken an ex ante assessment.
Source: EPRC Managing Authority survey.

Looking at the views of all MAs, ***among those who do have an opinion***, around 63 percent consider that ESI Funds and commercial banks complement one another, with 24 percent considering that they compete. For other sources of domestic funding, perceived complementarity is higher, with over 70 percent considering the sources complementary (and 16 percent considering that they compete).

An interesting finding is that where an ex ante assessment has been carried out, MAs generally perceive there to be more competition between ESIF FIs and other instruments. This is illustrated in Figure 5.4 which shows that ***MAs that have completed an ex ante assessment are more likely to take the view that ESIF FIs compete with publicly backed instruments at domestic or European levels.***

Figure 5.4: Do ESIF FIs compete with other instruments?



Notes: Managing Authorities, all funds, distinguishing those that have undertaken an ex ante assessment.
Source: EPRC Managing Authority survey.

Interviews with Managing Authorities suggest that, on the whole, ESIF FIs are considered to be additional and ***complementary*** to other domestic sources:

> "we are convinced that the application of FIs…will offer a supply of finance to selected beneficiaries that otherwise would not be available from private sources or other instruments programmed on the national level" (Regional Managing Authority interview).

> "there is always potential for competition but the ex ante should flush that out" (National Managing Authority interview)

> "funding opportunities were scarce in the private sector. In terms of the public sector, there were some other programmes but not really relevant for the aims of the FI" (Intermediate Body interview).

> "compatibility of FI financed from ESIF and national funds is ensured through monitoring committees" (National Managing Authority).

> "on the national level FIs are established for niches where private market players do not act and they aren't competing with one another. EU level funding sources are complementary for Member States funding." (National Managing Authority).

However, some noted the impact of the changed economic climate:

> "In the last year or two there has been too much liquidity on the market, therefore bank products financed from FIs are less relevant. There is competition between financial products for energy efficiency in housing." (financial intermediary interview).

> "To avoid competition with commercial funding you need constant monitoring of the implementation process to trace whether the market failures defined and being addressed are still in place" (financial intermediary interview).

And other considered there to be an overlap between policy tools at national and regional levels:

> "There are several instruments pursuing very similar objectives, which may result in some confusion for the potential recipients" (financial intermediary interview).

One area singled out by some where instruments funded from other sources could complement ESIF FIs concerns *large firms*, which are excluded from eligibility for ERDF and for which, in some Member States, domestic funding sources are insufficient.

5.2. What is the relationship between ESI Fund FIs and other EU sources of finance?

The relationship between ESI Fund FIs and other EU instruments of various kinds is less well understood than the relationship with domestic funding. It is evident that some European level sources of funding are simply not known to Managing Authorities, which explains why they were unable to express an opinion (see Figure 5.3). That said, there are strong indications that MAs perceive COSME to be in competition with ESIF FIs. As Figure 5.4 shows, over 10 percent of all MAs, and almost 20 percent of MAs where an ex ante has been done consider that COSME is in competition with ESIF FIs. When 'don't knows' are eliminated this figure rises to around 50 percent of respondents (irrespective of whether an ex ante has been completed).

Interviews with Managing Authorities confirmed the ***general lack of knowledge of other EU sources*** among some, especially at the regional level.

> "The landscape is really wide, perhaps even too wide. It is difficult to get a good (thorough) orientation." (Regional Managing Authority interview)

> "We do not have clear understanding of details concerning these instruments. Definitely lack of information. The information available is always general. For instance, it is always difficult to figure out what could be the costs of using these kind of instruments" (regional Managing Authority interview)

> "Specifically relating to the relationship between ESIF and EFSI, there is a perception that EFSI is relevant to large infrastructure-type projects, but less awareness of its activities in the field of SME support, for example." (Regional Managing Authority interview)

Box 5.2: ESIF FIs and EaSI

The ESIF regulations provide MAs with the option of making a financial contribution to FIs set up at EU level, managed directly or indirectly by the European Commission. This includes FIs which are part of the EU's Employment and Social Innovation (EaSI) programme. The EaSI programme is managed directly by the European Commission with the objective of promoting a high level of quality and sustainable employment, guaranteeing adequate and decent social protection, combating social exclusion and poverty and improving working conditions.[161] The programme has three axes; the third axis concerns Microfinance and Social Entrepreneurship and provides supports

[161] Regulation (EU) No 1296/2013 of the European Parliament and of the Council of 11 December 2013 on a European Union Programme for Employment and Social Innovation ("EaSI") and amending Decision No 283/2010/EU establishing a European Progress Microfinance Facility for employment and social inclusion.

the provision of microloans to vulnerable groups and loans to social enterprises via microcredit providers and social investors through FIs implemented by the European Investment Fund.

So far, the only OPs identified which have considered a contribution to EaSI financial instruments are in Spain - the national ESF OP for Employment, Training and Education and the ESF OP for Madrid. According to interview data, the financial allocation considered to the EaSI FI from the ESF OP for Employment, Training and Education would be approximately 15 percent of total OP funding (this would equate to just under €530 million). Within the Madrid OP, a separate priority axis has been created to contribute €25 million to EaSI. The contribution to EaSI is considered a pilot, to test out this new form of intervention for ESF.

Source: EPRC case study research – see Annex 1.

Financial intermediaries generally had a more comprehensive perspective on funding sources, but often agreed that the landscape was crowded and confusing.

> "A working group would be needed to in order to centralise and provide an overview of the different regional and national interventions and EU funding sources". (financial intermediary interview).

The advantages claimed for using FIs at EU-level include: potential multiplier effects; capacity building (national and local institutions benefitting from EU-level entrusted entities' know-how in relation to the design and implementation of financial schemes); ability of FIs to address market fragmentation; avoidance of duplication of effort; and minimised risks of failure in areas where it would be difficult for individual Member States to achieve the required critical mass. Making ESIF contributions to EU-level instruments may also save time and resources for the MA in the set-up phase, as use is made of the EU-level instrument delivery system. MAs are thus relieved of some of the administration related to design, tendering, and State aid compliance issues. Some, but not all of these claims are reflected in the view of Managing Authorities.

Where such mechanisms are familiar to MAs, there are different views on the relationships between the different sources, with some pointing to ***complementarity*** between EU funding sources:

> "The role of EFSI is complementary to OP financing. EFSI provides opportunities for attracting additional funding. At the moment possibilities to use InnovFin funding have been considered." (national Managing Authority)

> "The EU funding landscape is considered very appropriate. Each programme targets a specific funding gap. EFSI will play a significant role… but it still has to become fully operational since further marketing among the public and private sectors in needed." (Intermediate body interview).

> "A range of forms of support is regarded as positive. Synergies are sought with the EIB" (national Managing Authority interview).

> "There are several funding sources focusing on similar objectives. However conditions are too different and therefore they don't compete with one another" (national Managing Authority)

> "EFSI provides opportunities for attracting additional funding" (national Managing Authority)

Others noted an ***overall shortage of funding or an uneven distribution*** thereof:

> "Most of these [EFSI] funds are being absorbed by larger Member States. When planning the OP, possibilities to complement resources from other funds are taken into account. However, there are too few funding options which we could use." (national Managing Authority interview)

Among the potential challenges of using EU-level FIs are overlaps between FIs at European and national levels, lack of synergies among different kinds of expertise, and insufficient understanding of EU Regulations amongst actors involved. Moreover, managing authorities may have concerns over the lack of flexibility and control in the EU-level instruments, or over the added-value of allocating funds 'back up' to the Union level.

A number of respondents considered that, in general terms, various sources of EU funding ***overlapped****:*

> "EFSI, ESIF and Horizon 2020 can be used to fund similar project now this makes it very challenging" (Regional Managing Authority interview).
>
> "chaotic environment, where plenty of FIs are proposed quite frequently" (Managing Authority interview)
>
> "The positive point is a rich offer of funding options, the negative point is missing complementarity or even internal logic. (Managing Authority interview)
>
> "The EC insists on demarcation with grants while at the same time planning similar instruments on EU level as most of the Member States in national ESIF OPs. (national Managing Authority)

Some Member States have taken steps to address information and coordination issues:

> "There is overlap regarding the guarantee related FIs implemented on the EU level (COSME). A Co-ordination Board involving EIF, FoF etc. has been established."

And concern at the ***lack of understanding*** of the overall financial landscape with evidence of a lack of communication about other planned interventions:

> "..the EIF published a programme, the MA found out about it from the press and it was quite similar to the planned intervention…":
>
> "Some of the FIs implemented on horizontal level by the EIF and EIB (COSME, InnovFin) are similar in their structure to one implemented on national level. MS do not have a mechanism to receive an overview of their implementation and future planning".

However, there is also evidence of ***competition*** between EU level instruments and ESIF FIs and/or domestic financing, and a perception that ESI Funds are disadvantaged compared to other EU funding sources:

> "They should be complementary but they are not. There is competition." (regional managing Authority)
>
> "Indeed there is competition and overlaps – not necessarily under one OP but under ESIF and EU general programmes e.g. SME Initiative and COSME/InnovFin, microfinancing guarantees and EaSI. There is a clear overlap with a number of existing national schemes." (financial intermediary interview)
>
> "Competition is… found, though limited, between FIs established under the OPs and FIs co-financed by the EC, EIB, EBRD and other IFIs, for example targeted [at] SMEs under the OP and SMEs eligible for financing under the EC's co-investment facility. However, competition is believed to have a catalysing effect rather than threatening FI implementation and progress." (financial intermediary interview)

"EC level measures are in competition with national financing allocated to FI due to significantly better financing conditions (due to the fact that the EC-level measures are not considered as State aid). In accordance with the current regulation, national FI has no possibility to compete with the EU FI and ultimately may be partially rejected….

"…COSME and Horizon 2020 implemented FI are not considered as State aid and this gives a great advantage. FIs financed from ESIF are not so attractive." (national Managing Authority interview).

"The EU level instruments are somehow privileged – less regulatory burden put on them, compared to all the regulation concerning ESIF (national and regional instruments…. this does not help, rather complicates the landscape)

Figure 5.5: What are the incentives and disincentives of the various modes of intervention?

Mode	Incentives	Disincentives
ESIF financial instruments (ERDF ESF CF EMFF) under shared management (Off the shelf, tailor made)	• Control • Capacity to tailor to regional needs • Greater certainty over legacy	• Taking full responsibility for implementation • Regulatory complexity (especially State aid and procurement) • Lack of experience (EMFF, especially, also many ESF)
SMEI	• Co-financing • Delegation of responsibility • Administrative simplicity (procurement)	• Loss of control • Lack of regional differentiation for national SMEI OPs • No development of administrative capacity • Absence (so far) of successful pilots • Overlaps with other EU and/or domestic measures
Contributions to other EU level instruments (COSME, H2020, EaSI)	• State aid and procurement	• Loss of control • Lack of regional differentiation • Lack of knowledge • Administrative complexity • Lack of certainty over funding destination • Different accounting and audit systems

These concerns were shared by some financial intermediaries responsible for administering ESI Fund FIs:

"we are concerned about H2020, EIF are offering competition to our FIs…[we are] giving guarantees to banks. In the same way, EIF can give guarantees to banks. We cannot compete with them, they are offering better conditions to banks…. If there is not enough need for our guarantees now, we have to close down the product. If EIB suddenly leaves the market, then we do not have any alternative any more… European funds are competing against each other. EIF should not compete with us but supplement out schemes – they could give us the guarantees." (interview Financial intermediary).

"EIF – State aid regulations do not apply to them. Their conditions are much closer to the market. For banks it mean lower level of administrative burden and that is why they prefer EIF. But it is actually unfair treatment – for us one rule applies and to EIF total different ones." (interview Financial intermediary).

"There is a high risk of competition, especially in some regions with low absorption" (interview Financial intermediary).

"There has been cannibalisation in large projects" (interview Financial intermediary).

"FI delivered by EU institutions are State aid free and could be considered in competition with ones from ESIF" (interview Financial intermediary).

"In some areas – SME guarantees – they compete to a big extent" (interview Financial intermediary).

"Problem of guarantee instruments available from banks… competes with guarantee instruments based on EFSI" (interview Financial intermediary).

"They compete in the sense that there are strong lobbying groups who seek to maximise their own particular funding stream." (interview Financial intermediary).

"The main issue of concern relates to the different conditions in which ESIF FIs and EU level / EIB group instruments function. EIB/EIF are dealing with the same kind of FIs, but it's possible to implement them easier / faster as there are not so many constraining rules (whereas the rules for implementing ESIF FIs are much more onerous)… damages perception of ESIF FIs. Why are rules more onerous for ESIF FIs? (financial intermediary interview).

"There is a lack of institutional coordination for handling different funding options…despite significant efforts by COM to ensure complementarities… and despite the strong synergies rhetoric on paper… and this is projected onto the national level as well". (financial intermediary interview).

"EU level instruments don't provide incentives to financial intermediaries. There is competition on the ground e.g. SMEI and CIP [meaning COSME, probably]. EIB was already providing liquidity but market already liquid. In EFSI there is an opportunity, especially in infrastructure, but EFSI is offering 50% cover under InnovFin when there are already two banks offering 75% cover under EU-backed schemes. It doesn't make sense, it's politics and the need to have all MS participating in EFSI. EFSI is not market driven - the intermediary which took this on must have looser terms than under ESIF cofinanced FIs. It's sad because there is a gap in the market and it relates not to SMEs and H2020, where the market is very small, but on infrastructure where for example, EFSI could play a significant role in improving energy infrastructure in the Mediterranean, but it won't do that because it seems to be limited strictly to EU infrastructure." (financial intermediary interview).

5.3. What are the potential synergies between ESI Funds and other EU funds?

ESI Fund FIs and those funded from other others source overlap in some respects, but also address somewhat different objectives, as well as operating with distinct governance mechanisms and thematic targets. By way of example, the ESIF and EFSI funding are mapped against one another in Figure 5.6.

Against this background, issues which may hinder complementarity or synergies between the two sources have been identified:[162]

- the objective of EFSI is efficiency in targeting market failures and suboptimal investment situations; the aim is to fund economically and technically viable projects and as EFSI is a market driven initiative there are no territorial pre-allocations;
- concerns that ESIF funding will be crowded out by EFSI; and
- potential for conflict between applicable rules due to different legal frameworks.[163]

However, a recent survey among national actors,[164] suggests that some expected significant benefits, including:

- Increase of private sector investment (France, Finland and Poland);
- attract EFSI financing to leverage the EU Cohesion Policy funds (Lithuania);
- additional infrastructure and energy efficiency investments (Slovenia);
- opportunity to develop large scale and more ambitious projects either directly or indirectly affecting ESIF programmes (UK, Poland and Portugal) but also potential difficulties in terms of losing control over project (UK); and
- use of EFSI to mitigate the risk absorption of financial instruments to be created under the 2014-20 Operational Programme (Lithuania).

[162] Mendez C and Bachtler J (2015) Permanent revolution in Cohesion Policy: restarting the reform debate, European Policy Research Paper No.93, European Policies Research Centre, University of Strathclyde, Glasgow.

[163] European Court of Auditors (2015) Opinion No. 11/2015 (pursuant to Article 287(4) of the Treaty on the Functioning of the European Union) concerning the proposal for a Regulation of the European Parliament and of the Council on the European Fund for Strategic Investments and amending Regulations (EU) No. 1291/2013 and (EU) No. 1316/2013, Luxembourg.

[164] Van der Zwet A, Bachtler J (2016) Review of the Role of the EIB group in European Cohesion policy, report to the European Parliament, Directorate-General for Internal Policies

Figure 5.6: Similarities and differences between the EFSI and the ESIF

	EFSI	ESIF
Objectives	• To resolve difficulties in financing and implementing strategic, transformative and productive investments with high economic, environmental and societal added value contributing to achieving EU objectives. Finance projects with higher risk profile.	• Strengthening economic, social and territorial cohesion, particularly reducing disparities and backwardness of less-developed regions. • Contributing to Europe 2020 objectives.
Funding	• €16 billion (and €5 billion from the EIB) guarantee from the EU budget) with an expected leverage of 15 times (€315 billion of total investments).[165]	• €351.8 billion (dedicated EU budget heading), of which around €20 billion in indicative OP allocations to FIs.
Spatial targeting	• No geographical targeting / pre-allocations.	• Concentration on less-developed countries/regions through pre-allocated envelopes.
Thematic targeting	• No thematic pre-allocations/ring-fencing, although €5.5 billion (out of EUR 21 billion) reserved for SMEs. • Strategic infrastructure (including digital, transport and energy, education, research, development and innovation, renewable energy and resource efficiency) and support for smaller businesses and midcap companies.	• Ring-fencing of allocations to thematic objectives and investment priorities. • 11 thematic objectives (RTDI, ICT, SMEs, low-carbon economy, climate change, environment and energy, transport, social inclusion, education, training, employment, public administration efficiency).
Financial instruments	• Loans, guarantees, private equity and venture capital.	• Non-reimbursable grants, mainly Financial instruments (guarantees, loans, private equity and venture capital)
Forms of assistance	• Projects (of higher-risk profile than the EIB finances), financial instruments and/or investment platforms	• National and regional programmes. • Major projects (> €50m, funded by ERDF/CF and subject to Commission decision).
Management	• Centralised management by EIB with Steering Board including EIB and Commission representation • Financial intermediaries selected through open call	• Shared management between Commission, Member States and regions. • financial intermediaries are selected in compliance with public procurement law. There are situations where an open call is also possible (this will be the case eg where the manager of a FoF is the EIB/EIF or a body already selected through public procurement)
Project selection	• Project selection by EU-level Investment Committee of experts.	• Project selection by national and regional managing authorities and implementing bodies.
Timeframe	• 3 years (2015-18) with option for extension. Update!	• 7 years (2014-20).

[165] Note that there is currently a proposal to double EFSI both in terms of duration and financial capacity (COM(2016) 597 final) https://ec.europa.eu/transparency/regdoc/rep/1/2016/EN/1-2016-597-EN-F1-1.PDF

	EFSI	ESIF
State aid	• EFSI support does not constitute State aid	• Must comply with State aid rules – either no aid, de minimis, GBER or notification

Source: adapted from Van der Zwet A, Bachtler J (2016) Review of the Role of the EIB group in European Cohesion policy, report to the European Parliament, Directorate-General for Internal Policies.

Synergies with EU level instruments are being sought under several OPs, for example with Horizon 2020:

> "As the overall management of EU funds and programmes (H2020) is under the umbrella of the same regional ministry, they expect to reach a broad level of cooperation among different funds in the same strategy for economic growth".

> "The variety of funding options is overall positive. Companies have a choice and it is not difficult to navigate between the different funding options and determine what is appropriate… The procedures around H2020 are not very easy but still it offers considerable advantages." (financial intermediary interview).

However, interviews with Managing Authorities and financial intermediaries alike suggest that this is extremely challenging to achieve:

> "This phenomenon is more theoretical then practical."

> "To a large extent, programmes do not have a clear investment strategy, that is they are not tailored to a specific market/beneficiaries." (regional Managing Authority)

> "The vast amount of programmes creates confusion among potential beneficiaries" (regional Managing authority)

> "The OP is exploring options to include EFSI as part of an FI but this is proving to be very challenging. The main barrier is the different governance structures which are not compatible." (regional managing Authority)

> "The main problem of the large number of funding sources is to match projects with the most appropriate sources" (regional Managing Authority)

> "Due to the lack of information on the particular programmes potential synergies are unclear" (national Managing Authority)

> "Don't find any real correlation or joining up. These things exist… they try not to compete or duplicate… ex ante helps… but it is clear that the Commission should have thought about it from the outset instead of retrofitting synergies." (interview financial intermediary)

> "Commission DGs all set up their own standalone programmes which all have slightly different objectives but overlap" (interview financial intermediary)

> "Too many funds, too many providers, too complicated. EIB could play an important role in simplifying the funding landscape" (interview financial intermediary)

> "Potential for synergies is high but there is a lack of guidance for the establishment of joint initiatives" (interview financial intermediary)

> "the landscape seems to have been the result of evolution rather than firm design" (interview financial intermediary)

> "In principle EU programmes are complementary, but in practice it is not so. Rules should be more homogenous in order to achieve complementarity. Juncker plan bring even more complexity: huge mass of funding which follows a different model. The SME instrument under H2020 is overly complex both in terms of eligible subjects and in terms of State aid compatibility. The SME initiative may have a positive effect for banks, but less so for businesses… the approach in general is less calibrated for specificities of territories." (financial intermediary interview).

"At the moment, the key obstacle is the missing legislation that would provide conditions for matching various sources of funding" (financial intermediary interview).

6. CONCLUSIONS, RECOMMENDATIONS AND POLICY OPTIONS

The overarching aim of this study has been to assess how to improve the take-up and effectiveness of Cohesion policy financial instruments through the following key tasks:

- Setting out the rationale for the use of financial instruments, taking account of the diverse economic contexts
- Describing how Member States are making use of financial instruments in 2014-20
- Identifying practical, legal and administrative capacity issues which influence the uptake of FIs
- Analysing the relationship between Cohesion policy FIs, EU level instruments and those managed by the EIB Group, especially EFSI.

The study has involved an extensive review of the academic and policy literature, a 'stocktake' of FIs providing a snapshot of Managing Authority plans and progress by spring 2016, an online survey of Managing Authorities, and around 130 interviews with Managing Authorities, Intermediate Bodies, financial intermediaries, and European Commission and EIB group officials.

The aim of this final section of the report is to provide conclusions on the strengths and weaknesses of the legislative framework established at EU level for the use of financial instruments, to identify specific recommendations for possible improvements and to set out some options for the future regarding the legal framework and the uptake of financial instruments co-financed by ERDF, Cohesion Fund, ESF and EMFF.

6.1. Conclusions

Cohesion policy plans for 2014-20 are being implemented in a climate that is ***overshadowed by the aftermath of the crisis***. A key factor in the weakness of the recovery has been the impact of the financial and economic crisis on public and private investment. In spite of historically low interest rates, investment has stagnated for much of the last decade in response to persistent uncertainty and low demand, fuelling concerns over the long-term future of the European economy. At national level, patterns of public and private investment vary widely. In some countries, public investment has shrunk dramatically since the crisis, while in others, probably partly due to Cohesion policy receipts, public investment has increased. Similarly, while in some countries private investment exceeded pre-crisis levels by 2015, in most countries private investment in 2015 was lower than in 2007 in real terms. More generally, public investment has been constrained by the impact of government spending in response to the crisis and private investment has been held back by uncertainty about the longer term implications of the sovereign debt crisis and the general weakness of economic activity.

In spite of this uneven investment context, there is some consensus that there is ***no generalised problem of access to finance*** – in fact, listed European companies have very large cash holdings; however, access to finance remains ***a serious concern for some firms and activities.*** In particular, small and medium-sized and innovative firms remain affected by financing constraints, partly owing to their reliance on bank lending which was curtailed as banks rebuilt their balance sheets and took more cautious approaches to risk. Moreover, there are infrastructure needs across Europe which face significant financial challenges because bond markets have dried up and private long-term financing has become more difficult to secure. It is this perception that underpinned the establishment of EFSI.

Clearly domestic sources of finance can and do play a significant role in addressing these issues. In this context it is worth emphasising that many Member States make extensive use of FIs in domestic policy and in some, Cohesion policy essentially enhances the budgetary capacity of existing initiatives by adding another credit line or block of finance within an institution. Generally, however, it is ***difficult to assess the scale of domestic public sector finance*** in pursuit of economic development goals: the institutions delivering public sector FIs vary widely in structure and function and the sources and terms of finance are not always transparent or distinct, let alone comparable. At the same time, the sector is undergoing change with the emergence of ***new national promotional banks*** (NPBs) in a number of countries against the backdrop of the difficult investment climate. The ***overall landscape is made more complex by the role of EU institutions***, which are increasingly involved in the supply of FIs both in their own name and through intermediaries operating domestically (including NPBs). The number, range and remits of domestic intermediaries, coupled with a lack of transparency in the ultimate source of funding – partly owing to 'rebranding' - makes it difficult accurately to assess the scale of funds available and obscures the genuine additionality of ostensibly new funding streams.

Against this background, what then is the ***rationale for financial instruments in Cohesion policy***? There are arguably several dimensions to this. The underlying question is what the ***justification for public intervention in any form?*** The response to this is generally cast in terms of the need to support activities that the market cannot or will not undertake alone, but which are considered to be in the public interest. This can arise where there simply is no market (for instance public goods and some merit goods) and the private sector is operating quite rationally, or where the market is imperfect or operating sub-optimally. A second issue concerns the ***form of intervention***. Repayable funds are *an alternative delivery mechanism* to grants (and not just a means of addressing a finance gap). However, financial instruments are only feasible where the investment is ***income-generating***, enabling the initial support to be repaid. This means that where public intervention is justified by the need for public goods, repayable support is unlikely to be well-suited. Three ***principal arguments for using financial instruments*** instead of grants are conventionally highlighted in the context of Cohesion policy. First, FIs are more ***sustainable*** because funds are repaid, creating a legacy to invest again. Second, FIs can improve ***project quality*** – this may be partly through the due diligence involved in private sector project assessment, but also because having to repay support focuses the recipient on project viability. Third, FIs can be more ***cost-effective*** partly because funds may be recycled, but also because of their potential to attract private funds.

These arguments have largely underpinned Commission ambitions ***to double the expenditure on FIs*** in 2014-20, though it should be stressed that while these benefits are increasingly accepted as conventional wisdom, it is also clear that ***financial instruments are not suitable for all types of intervention, nor relevant to all Cohesion policy programmes***.

Direct comparisons between funding periods are not straightforward, but initial indications are that ***Member States are broadly on target*** to meet the goal of doubling FI spend with planned ESIF commitments of around €21 billion. However, the proposed use of FIs ***falls short of the indicative targets by investment area***: this is met only in the case of R&D&I where 8.9 percent of ESIF spend is planned to be in the form of FIs, as against the target of five percent; for SMEs the target was 50 percent, but just 34 percent of ESIF spend is planned on FIs. In the case of sustainable transport, some 0.3 percent of the ESIF total is planned to take the form of FIs, against a target of 10 percent.

Overall, it can be seen that Member State ***plans for FIs are consistent with the theoretical rationales for financial instruments.*** Over 87 percent of planned FI spend is on TO1 (R&D&I - 17 percent), TO3 (SMEs – 52 percent) or TO4 (low carbon – 17 percent) – areas where there are known market imperfections (such as informational asymmetries, risk aversion or long term financing needs). The broad nature of the Thematic Objectives makes it difficult to assess whether, in principle, there is greater potential for the use of FIs than planned by Managing Authorities, but the stated ***reasons for the 'non use'*** of FIs are instructive, especially in relation to those TOs where they are widely used. Overall, the main reasons for *not* using FIs is that they are deemed unsuitable for planned projects, likely reflecting, at least in part, the fact that many projects involve public or merit goods that are not revenue-generating. However, in the case of TO3 (SMEs) and TO4 (low carbon) the single most important reason given was lack of demand from final recipients, with 'insufficient critical mass' (i.e. the OP being too small) and 'lack of administrative capacity' also prominent. These reasons are interesting, but each raises further questions: (i) Why is there a lack of demand: does this reflect a 'grant culture', a lack of confidence to invest, or the need to develop 'investor-ready' projects through other forms of intervention? (ii) If the OP is too small, is there a 'tier' of funding or pooling mechanism that could be relevant? (iii) If administrative capacity is lacking, how best can this be addressed?

In considering the ***strengths and weaknesses of the legislative framework generally***, views are rather mixed and not always easy to reconcile. A widespread criticism of the 2007-13 legal framework for FIs was that it was too sparse. The provisions relating to financial instruments in the 2007-13 Structural Funds regulations were very limited in detail. A series of COCOF notes provided additional detail, but were criticised for being slow to appear, unclear in their status and retroactive in application. The regulatory provisions for financial instruments have been strengthened significantly in 2014-20 and while many Managing Authorities and financial intermediaries welcome the increased precision, others have criticised the new rules for being too detailed and complex. Managing Authorities have not always found the sheer number of different texts easy to navigate and have been critical of the delays in their adoption. Moreover, as well as introducing additional detail, Managing Authorities also widely perceive that the rules relating to selection of intermediaries were changed, which ***has made continuity difficult even for FIs that were working well in 2007-13.***[166]

A more general issue among Managing Authorities, whether users or non-users of financial instruments is that FIs are perceived to be ***complex to administer***. Moreover, ***MAs with experience of both grants and FIs consider FIs to be considerably harder to administer*** (though some MAs also note that part of the burden can be delegated to financial intermediaries). The complexity of the rules, and their lack of clarity in places, coupled with the need for certainty fuelling demand for explanatory guidance, has proven a disincentive for many and a source of frustration for Managing Authorities that do pursue the use of FIs. In general, Managing Authorities tend to be risk-averse in applying Cohesion policy rules since payment suspensions resulting from transgressions are viewed as politically embarrassing and can affect the capacity of the programme to draw down the allocated funds. This raises the issue of the ***relationship between guidance and audit***, with many Managing Authorities concerned that documents intended only to clarify or illustrate good practice are being elevated to mandatory status by auditors.

Turning to some of the specific elements of the new rules, the ***requirement for an ex ante assessment is widely welcomed***. That said, some expressed concern at the prescriptiveness of the methodology and doubts about the ability of such an analysis to capture changing economic conditions and market needs on a long term basis. There are also questions over the validity of the market assessment in the absence of a

[166] The Commission contends that full compliance with the procurement rules was already required in 2007-13; nevertheless, Managing Authorities perceived this as a rule change and adapted their behaviour.

comprehensive overview of FIs given the emergence of new initiatives at EU level or under EFSI, of which Managing Authorities are often ignorant.

So-called ***'off-the-shelf' instruments*** were eagerly anticipated by many as providing solutions to State aid compliance and procurement issues. In practice, the uptake has been low, and this for several reasons. First, many Managing Authorities planning FIs in 2014-20 had used them in 2007-13 and had gained sufficient experience not to need a 'template'; partly related, for others the OTS models simply came too late. Second, State aid compliance in the first batch of OTS instruments is on the basis of *de minimis* support to final recipients; this may be less generous than aid on GBER terms and carries with it a considerable administrative burden that not all Managing Authorities are willing to carry. Third, the terms are not always sufficiently attractive to financial intermediaries with respect to risk-sharing.

The new Regulations increased the ***range of implementation options*** and whilst this is generally welcomed, it also raises some issues about the relationship between different instruments and institutions, particularly in the context of new EU horizontal instruments and EFSI. These issues relate to both principle and detail. At a detailed level, perceptions of the EIB Group are mixed: some consider that their role in procuring intermediaries has been very valuable, but others express some resentment at the privileged position of the EIB Group in relation to domestic financial intermediaries in terms of their administrative burden and the lack of transparency in their mandate. There is also a perceived potential conflict of interest in the role of the EIB Group in providing both training and marketing its own products and activities. More generally, the uptake of the SMEI is widely viewed to have been more a result of political pressure rather than policy need, with some raising concerns at the relationship between SMEI and other support for SMEs, the lack of guidance on the role of the MA in relation to SMEI, and the risk that EU level instruments can inhibit the development of administrative capacity within the Member States.

This leads on to a more general concern about the number and range of instruments with different geographies and governance systems, but operating in similar or overlapping markets. Evidence from this study suggests that ***the relationship between ESIF FIs and other EU instruments of various kinds is not well understood*** especially by Managing Authorities. This partly arises from the fact that Managing Authorities, certainly at regional levels, are much less likely to engage with instruments such as EFSI, or even SMEI, where decisions about whether to use such instruments are often taken at national level and involve more politicised decision making. That said, Managing Authorities that have completed ex ante assessments (and therefore likely to have greater experience of FIs) are *more* likely to consider that there is competition between ESIF FIs and other EU instruments than are MAs that have not undertaken ex ante assessments. Financial intermediaries tend to be more familiar with the financial instrument landscape than MAs, and whilst some view the range of options as encouraging healthy competition, many are critical of the overlap, the differences in terms and conditions (e.g. in relation to State aid) and the resulting confusion 'on the ground.' In any event, experience of combining financial instruments from different sources remains rather limited, though there is evidence of considerable complexity, and delays, especially over State aid issues, when this has been pursued.[167]

[167] Ménard, L. (2017) *Plan Juncker et règlementation des aides d'Etat,* séminaire sur les aides d'Etat en faveur des infrastructures, Ecole Militaire, Paris.

6.2. Recommendations

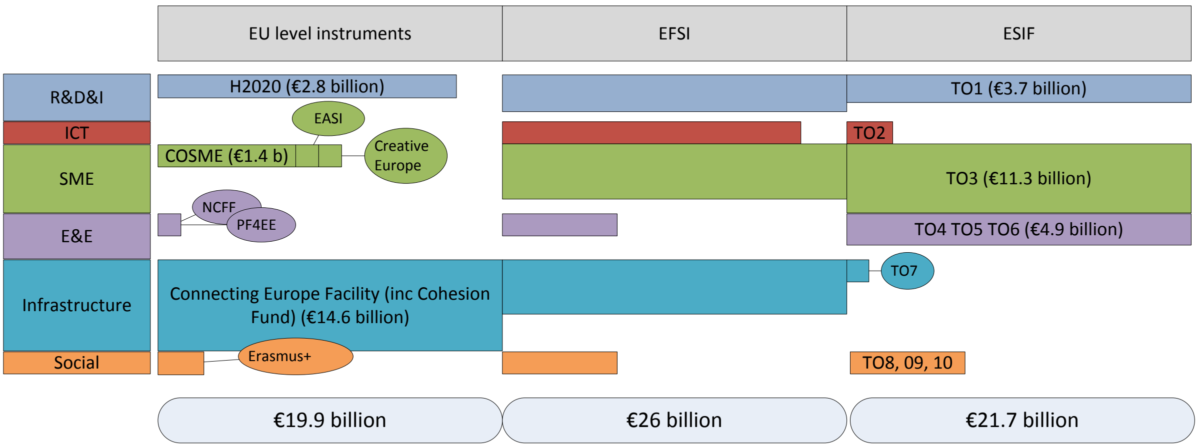
Against the background of these broad conclusions, a number of recommendations can be put forward, while acknowledging current Commission proposals for a so-called 'omnibus' Regulation, which seeks to address some of these issues. These recommendations fall under three broad headings: a reappraisal of the roles of ESIF cofinanced FIs, EU level instruments and other initiatives; greater regulatory stability; and the refocusing of guidance and support.

6.2.1. A reappraisal of the roles of ESIF co-financed FIs, EU level instruments and other initiatives

Concern at under investment in the European economy has led to a number of EU level initiatives for financial instruments addressing a range of objectives, including SMEs, infrastructure and R&D&I; at the same time, EU Cohesion policy objectives have widened to embrace Europe 2020 aims, while budgetary pressures and concerns with efficiency have emphasised the use of financial instruments as a Cohesion policy tool, with an extended range of implementation options.

The net outcome is a complex pattern of financial instruments of very varied types and scale, which may complement one another, but also overlap and compete. The tendency to 'rebrand' EU initiatives when implemented nationally, or to incorporate existing initiatives within another 'wrapper' or 'window', as under EFSI, contributes to the difficulty in establishing the exact scale and source of the funding available. At the same time, political pressure to take up certain instruments and ensure a given geographical spread can result in the proliferation of measures at the point of delivery with distinct regulatory and other requirements, but ultimately similar policy objectives and arguably limited additionality.

Figure 6.1: Estimating the scale of EU FIs by source and objective



Notes: The boxes representing budget commitments are broadly to scale. In the case of EFSI, the breakdown of commitments as at November 2016 has been used as a proxy to disaggregate the commitment by objective for illustrative purposes, though clearly the past may not be a guide to the future.
Source: EPRC calculations based on Regulations underpinning the various initiatives and OP budget commitments for ESIF.

Against this background, there is a need to consider the respective role of different instruments and improve the legibility of the financial instrument roadmap. 'Synergies' have become the holy grail of policy implementation, but the practicalities involved in achieving them are onerous, with different instruments driven by different regulatory requirements so that only the most determined, and those with the requisite administrative capacity, are likely to be willing and able to achieve the coordination required.

Cohesion policy FIs offer strengths and weaknesses in this environment. Among their strengths are the capacity to adapt to local conditions, develop regional financial markets and improve the geographical equity of spend – there is a tendency for horizontal instruments to be demand-driven, with uptake higher in the more prosperous regions and to be unresponsive to local needs. Cohesion policy FIs also have weaknesses – some of the regulatory aspects demand significant administrative capacity and some monitoring and reporting requirements, as well as constraints on management costs and fees, risk being a disincentive to the involvement of financial intermediaries. At the same time, many Cohesion policy FIs are small and may lack the critical mass needed to be effective, and cost-effective.

In this context, some have promoted the SMEI as a 'hybrid' option which avoids the State aid and procurement issues faced by tailor-made instruments, and yet allows a degree of adaptation to specific conditions. However, it is premature to draw conclusions on the performance and satisfaction with SMEI as time is needed to understand to what extent SMEI meets regional requirements, and / or potentially undermines capacity building.

In parallel, it is open to question whether it is realistic or desirable to seek to increase further the use of FIs in Cohesion policy, especially in areas that come within the realm of horizontal policies and when the scope for comparatively large numbers of standardised applications (as is possible in the areas of SME support and to some extent energy efficiency) is limited. However, this of course touches on the more fundamental issue of the role of Cohesion policy in delivering sectoral elements of the Europe 2020 agenda, a question which is beyond the purview of the present study.

6.2.2. Greater regulatory stability

For many Managing Authorities and regional economies, the use of FIs in Cohesion policy represents an important cultural shift away from grant-based intervention. In this context the regulatory challenges have been significant – sparse rules and limited guidance in 2007-13, followed by detailed rules and delayed guidance in 2014-20. Many Managing Authorities are increasingly convinced of the merits of FIs in appropriate circumstances, but frustrated by the complexity of the rules and their revision on a seven-year cycle.

Against this background, there is *a compelling argument for regulatory stability*, enabling policy practice to develop to meet regional economic needs, rather than being dominated by concerns with compliance; in both the 2007-13 and 2014-20 policy cycles, discussions about the effectiveness of financial instruments have been overshadowed by issues of compliance and process, rather than policy design and a focus on 'what works in what circumstances' to address specific economic development objectives.

The proposed omnibus Regulation[168] is designed to address a number of specific issues in the rules on financial instruments, notably, in the present context, in relation to

[168] European Commission Proposal for a Regulation of the European Parliament and of the Council on the financial rules applicable to the general budget of the Union and amending Regulation (EC) No 2012/2002, Regulations (EU) No 1296/2013, (EU) 1301/2013, (EU) No 1303/2013, EU No 1304/2013, (EU) No 1305/2013, (EU) No 1306/2013, (EU) No 1307/2013, (EU) No 1308/2013, (EU) No 1309/2013, (EU) No 1316/2013, (EU) No 223/2014,(EU) No 283/2014, (EU) No 652/2014 of the European Parliament and of the Council and Decision No 541/2014/EU of the European Parliament and of the Council, COM(2016)605 final of 14 September 2016.

contracting directly with national promotional banks for the implementation of FIs and facilitating the application of only one set of rules in the case of combinations of measures (such as ESIF and EFSI). However, there is a strong case for resisting further tinkering and allowing policy to bed down, enabling policymakers to focus on how well policy is working and to facilitate policy learning over several programming periods, rather than 'relearning' policy frameworks with each new cycle. As part of this, thought could be given to the scope to roll forward as seamlessly as possible those instruments which are considered to be performing well, without, for example, imposing a need to re-procure financial intermediaries just to coincide with the OP planning cycle. A further move that would enable the rapid set-up of FIs would be to undertake the ex ante assessment for FIs in parallel with the ex ante evaluation of OPs, which would also help avoid situations in which grants can be made available more quickly.

6.2.3. Refocusing guidance and support

Partly related to the second recommendation, there is a case for shifting the emphasis of guidance and support. The more detailed guidance provided in 2014-20 has generally been appreciated by Managing Authorities and financial intermediaries, but has also been criticised on several counts and steps could be taken to refocus support to target specific implementation needs, especially against the backdrop of regulatory stability.

First, in the 2007-13 and 2014-20 funding periods FI guidance has not been timely, but has often been published considerably later than the regulatory frameworks to which it relates. This creates uncertainty and / or delays in implementation since Managing Authorities must decide whether to proceed in the absence of guidance or await specific instruction. Greater stability in the regulatory framework would facilitate the simultaneous publication of the rules and guidance.

Second, and related, the status of guidance and the role of audit need to be clarified. The presence of guidance can be double-edged – the absence of guidance implies scope for discretion, but once guidance is available there is a widespread perception that auditors treat the content as mandatory, even where it may simply be intended to be illustrative or reflect good practice.

Third, financial instruments have become prominent in the EU economic development toolkit, but the term embraces mechanisms that are very diverse in objectives, scope, scale, design and governance. At the same time, administrative capacity and experience differ considerably. This implies the need for more tailored support, including: the development of off-the-shelf instruments that address a wider range of needs; targeted coaching and exchange of best practice, notably in specialised fields or under the ESF or EMFF where there is less experience to date; and more direct communication between Managing Authorities and the Commission to address specific issues.

6.3. Options

The broad thrust of the recommendations outlined above is to consolidate, coordinate and stabilise the regulatory framework for financial instruments and to support the development of administrative capacity in Managing Authorities. Of course, it is also possible to countenance more radical options for increasing the uptake and effectiveness of financial instruments. The discussion below outlines some such options for different dimensions of financial instruments – regulatory, governance, budgetary – some of which have the scope to be combined with others. These are summarised in **Error! eference source not found.**.

Figure 6.2: Options for improving the uptake and effectiveness of FI?

Option	Key features	Key advantages	Key disadvantages
1. Status Quo	Maintain current regulatory framework essentially unchanged	Stability and familiarity with existing arrangements	Knowingly retains some acknowledged weaknesses
2. Status Quo Plus	Maintain current regulatory framework, but align State aid and procurement rules for all FIs (shared management and EU level)	Creates a level playing field for ESIF FIs	Competition rules could be undermined, with wider implications, notably the risk that non-cofinanced domestic instruments may be disadvantaged
3. Upfront Decisions about Delivery Mode			
a) Off-the-shelf options only	Only FIs following an approved 'template' (of which there may be a wider range) would be eligible for co-financing	Ease of regulatory compliance, comparability and transparency	Insufficiently responsive to local contexts; difficult to justify on grounds of subsidiarity
b) Delegation of all ESIF funded FIs to EU level	ESIF to be used in the form of FIs would be reallocated to EU level instruments	Reduces administrative burden on Managing Authorities and rationalises patchwork of FI measures; facilitates consistency in compliance and implementation	Difficult to justify on grounds of subsidiarity; creates superfluous financial circuits
c) Ring-fencing ESIF spend for FIs	Earmark a minimum absolute amount or share of ESIF allocations to take the form of FIs	Forces a more imaginative consideration of how FIs could be used (in order to avoid loss of ESIF)	Arbitrary approach which is difficult to reconcile with ex ante assessment requirement and could encourage inappropriate spend
d) Use of grants only under ESIF	Only deploy ESIF in the form of grants, leaving FIs for domestic policy or EU instruments	Reduces administrative burden on Managing Authorities and rationalises patchwork of FI measures	Renders ESIF and its cofinancing less sustainable; restricts the range of projects under OPs and/or involves a shift back towards a 'grant culture'
e) Presumption in favour of FIs	A presumption that support for revenue-generating projects would be in the form of FIs, implying an ex ante assessment for grant interventions	Makes FIs rather than grants the default policy delivery option	Risks becoming a 'tick box' exercise and systematic ex ante assessment of grants would be a substantial exercise

6.3.1. Status Quo

The discussion of policy recommendations above made a strong case for policy stability in the context of financial instruments, arguing that regulatory change and adaptation to the new more detailed rules and guidance needed time. As such, essentially maintaining the ***status quo*** for the next programming period is clearly an option to which consideration should be given. Some of the ***advantages*** of retaining the status quo have already been outlined:

- This could enable a re-focusing of attention on the content and substance of policy and 'what works well in what conditions', in place of the dominance of policy debates by process and compliance considerations.
- It would also facilitate policy learning between programming periods, enabling policy properly to 'bed down' rather than being uprooted by further regulatory change. Even experienced MAs have found it difficult dealing with changes in the regulations between periods.[169]
- It would mitigate much of the delay involved in implementing FIs (which ironically can serve to render grant-based support more attractive) since it would enable ex ante assessments of FIs to be conducted in parallel with ex ante evaluations of the Operational Programmes. The ex ante assessment process has been found to be time-consuming and add to implementation delays.[170]

The ***disadvantage*** of simply rolling forward the status quo is that, as this report has shown, Managing Authorities and others have expressed a range of concerns at the current rules (including the level of detail, complexity, and problems around interpretation)[171], and the new regulations provide an opportunity potentially to simplify the implementation of ESIF cofinanced FIs instead of perpetuating known shortcomings.

6.3.2. Status quo plus

Following logically from the *status quo* option is a ***status quo plus*** option. Under this approach, the basic tenets of the current system would be retained but changes made in order to 'level the playing field' between financial instruments operated under shared management and those operated at the EU level, while addressing the perceived complexities in the shared management approach. The key areas of concern that have emerged from this study have been in relation to procurement of financial intermediaries and the State aid rules.

In relation to procurement of intermediaries, the EIB group is perceived to benefit from a privileged status through its preferment in the Common Provisions Regulation;[172] at the same time, some consider there to be a conflict of interest between EIB's status as a European institution and its essentially commercial activities which are heavily marketed to Managing Authorities. This is viewed as unfair competition.[173] Concerns at the uncertainty surrounding the selection of intermediaries may be partly assuaged by the so-called 'omnibus' proposals mentioned earlier, which, among other things, aim to clarify the circumstances in which Managing Authorities can directly award a contract to a national promotional bank. However, at the time of writing, these proposals had not yet been agreed.

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[169] See page 106.

[170] See page 107.

[171] See pages 105-106.

[172] Article 38(4)(b).

[173] See page 127.

The second area where the 'playing field' is perceived to be tilted concerns State aid. In spite of the 'off-the-shelf' Regulation and the expanded General Block Exemption Regulation, State aid compliance remains of major concern to Managing Authorities. This is partly because MAs tend to be risk averse - the consequences of State aid compliance errors can be serious for final beneficiaries and final recipients, both of which may become unwitting recipients of incompatible State aid unless measures are carefully designed. In addition, many Managing Authorities consider that audit authorities are too cautious in their approach, due to lack of knowledge on both financial instruments and State aid issues. At the same time, where the EIB Group acts under a mandate from the European Commission and manages EU funds, Union financing does not qualify as State aid; substantive and procedural requirements of the State aid rules do not apply to the extent that there are no resources from or under the control of Member States.

The main ***advantage*** of addressing procurement and State aid issues in ESIF FIs is that simplification of the regulatory requirements could encourage FI uptake and mitigate actual or potential competition between policy instruments deployed under different modes of governance. At present, procurement and State aid issues are among the most challenging for many Managing Authorities, and complexity and lack of uniformity between definitions and regulations is discouraging uptake of FIs.[174] The Omnibus Regulation proposal takes some steps on both these issues. As mentioned, it aims to clarify the selection criteria for national promotional banks as financial intermediaries; in addition, it also proposes to align State aid compliance where ESI funds contribute to EU-level financial instruments and eliminate double verification in such instances. However, no provisions are made in respect of State aid compliance for ESIF FIs implemented under shared management.

The ***disadvantages*** of this option concern its wider implications. Alignment of the State aid and procurement rules for ESI Fund FIs with those for EU level FIs would either involve discrimination between domestic instruments with and without ESIF cofinancing, or call into question firmly embedded aspects of State aid and procurement rules. This would not only be complex to implement but could also run counter to the established decisional practice of the Commission or European Court case law.

6.3.3. Upfront decisions about delivery mode

Aside from the overarching framework within which FI design is set, there is potentially a number of specific options about how FIs could be implemented and governed, and what their scale or role might be in the overall operational programme - see Figure 6.2. These are now explored in more detail.

a) Off-the-shelf options only

One option for addressing the perceived regulatory complexity of FIs would be to deploy ESIF cofinanced FIs only through ***off-the-shelf*** (OTS) instruments. This would mean that FIs had to conform to a given template in order to qualify for ESIF co-financing. Off-the-shelf instruments were eagerly awaited by many Managing Authorities, but so far, it appears that no Managing Authorities have actually used this implementation option directly. That said, there is evidence that OTS models are used 'as inspiration' for bespoke solutions. Moreover, Managing Authorities were not *generally* negative about off-the-shelf models and many would consider using OTS templates in future. However, in order to increase their uptake, it is likely that the range of OTS models would require to be expanded, for example, to include options with more generous terms than *de minimis* solutions to State aid or reducing the risk borne by private investors to improve the attractiveness of certain models.

[174] See page 113.

Restricting the implementation of ESIF FIs to those based on OTS models could offer a number of ***advantages***:

- The foremost advantage would be ease of regulatory compliance. Because of the requirement to use the template, uncertainties would be eliminated and the audit process eased. Their potential to speed up implementation and facilitate management is widely accepted.[175]
- Additional benefits could derive from the transparency of the mechanisms involved, which would be more readily understood, and the comparability between jurisdictions.
- This could potentially facilitate lesson-drawing between jurisdictions, making it easier to evaluate 'what works' in what context and adjust future policies accordingly.

This approach would also have a number of ***disadvantages:***

- It would be difficult to justify the imposition of off-the-shelf models on Managing Authorities that had already found adequate tailor-made solutions. Indeed, the main reason cited by MAs for not using OTS FIs was a preference for building on their existing FIs, primarily because the available OTS models available did not meet the identified needs of the OP.[176]
- There is also a wider subsidiarity principle to consider – OTS models aim to facilitate the implementation of financial instruments, but it is difficult to justify using them to *constrain* how FIs are implemented when non-OTS solutions are also viable and may be better suited to local conditions; MAs preferred to implement FIs tailor-made to meet regional or national needs.[177]
- The administrative burden at the level of the Commission; developing the current suite of models was a time-consuming and protracted exercise, involving extensive stakeholder and expert consultation. Among the reasons for the low interest in OTS is their lack of flexibility, suggesting that a wider range of models needs to be developed to increase their uptake. This task would involve significant work for the Commission, with the added challenge of providing a range of OTS models in a timely fashion ready for rapid deployment in the new planning period.
- While OTS models are suitable for circumstances in which there a significant numbers of relatively standardised projects – such as in the areas of SME support and energy efficiency in residential buildings – there are other areas where a bespoke approach is required and insistence on the use of OTS models might unwittingly exclude imaginative or innovative projects. A range of potential new OTS models were suggested by MAs.[178]

b) Delegation of all ESIF funded FIs to EU level

A further option to address some of the regulatory issues under ESIF cofinanced FIs would be to ***delegate all financial instrument implementation to the EU level***. In effect, this would extend and make mandatory the current provisions in the CPR under Article 38(1)(a) and Article 39. As such, the role of the Managing Authorities in FIs would

[175] See page 100.

[176] See pages 100-101.

[177] See page 101.

[178] See the case study on OTS instruments in Section 1.6 of Annex I. Suggestions included a securitisation instrument, support for R&I, especially for research and science institutes, environmental protection, microfinance lending and venture capital investment for high risk start-ups, as well as a model specifically tailored to the needs of the fisheries sector, a model for energy renovation of public sector buildings, and a model suitable for use with ESF Fis.

be much more limited in relation to FIs and essentially involve instructing ex ante assessments (and even this could be delegated 'up') and deciding what proportion of OP resources to commit to which instruments; they would cease to be involved in the practical implementation.

The key ***advantages*** of this option are:

- This would simplify the tasks of Managing Authorities in key areas of FI implementation, notably State aid and selection of financial intermediaries, but also audit. It would facilitate compliance with State aid and procurement rules because of the role of the Commission (under Horizon 2020 or COSME, for example) and of the EIB group (under the SMEI, or similar instruments).
- This approach could also help to rationalise the patchwork of measures across the EU by providing more consistent and comparable implementation of FIs, as currently there is concern about overlap and competition between the different initiatives, as well as a perceived lack of communication and transparency about new initiatives.[179]

This approach also has a number of ***disadvantages:***

- Experience with the use of ESIF cofinanced EU level instruments and SMEI is rather limited to date,[180] and it would be difficult to justify restricting FI implementation to models that have been little used.
- As with imposing OTS models, it would be difficult to justify on grounds of subsidiarity especially, but not only, where Managing Authorities had found adequate solutions to implementing FIs suited to local contexts and institutional settings.
- This approach would essentially add a further financial circuit to EU spend, with limited value-added.

c) Ring-fencing of support for financial instruments in ESI Fund allocations

Beyond the regulatory and governance options, there might be scope to encourage the uptake of FIs by ***ring-fencing ESIF spend for financial instruments***. This could take the form of earmarking an absolute minimum amount or share of ESIF allocations to be spent in the form of financial instruments. This could be done at Member State or OP level and/or could be at the level of thematic priorities/investment areas.

The main ***advantage*** of earmarking or ring-fencing sums for FIs is that it would force a more thorough, and potentially more imaginative, consideration of where and how financial instruments could be used. National authorities and/or Managing Authorities would have a particular incentive to maximise the use of FIs, or at least ensure that the 'quota' was met, since the funds might otherwise be lost.

The ***disadvantage*** is that such earmarking is likely to be arbitrary by nature. There is no real basis ex ante for determining that a given share or amount of ESIF should take the form of financial instruments. Indeed, this runs counter to, or potentially undermines the role of the ex ante assessment for financial instruments, the purpose of which is to determine what level of funding and form of support is appropriate. This in turn would be a backward step since the introduction of obligatory ex ante assessments is widely

[179] See pages 125-126.

[180] See Section 5.2.

viewed as the most positive innovation in FI implementation in 2014-20, being viewed as a useful tool for assessing market needs.[181]

d) Grant only support under ESI Funds

A related option would be simply to cease using FIs and ***only deploy grants under ESIF***. This might also imply a shift in the composition of ESIF co-financed interventions to focus more on public goods, non-revenue generating projects and areas where there is demonstrably no market as such, in short, refocusing ESIF support on interventions where grant funding is necessary. On the other hand, if similar priorities were pursued (such as SME support and low carbon economy), it might involve a return to supporting these wholly through grant-based mechanisms. As such, financial instruments would be deployed through domestic and EU level mechanisms to appropriate investments, but not with ESI Funds.

The main ***advantage*** of this approach, as with several of the other options, concerns the reduction of the administrative burden on Managing Authorities, especially in the key areas of State aid and selection of intermediaries. Such an approach could also help rationalise the FI landscape and make ESIF intervention more focused and distinctive. This applies particularly to the ETC programmes, where FIs have been found particularly difficult to integrate into the 'cooperation' approach.[182]

This approach would also have several ***disadvantages:***

- It could restrict the range of interventions supported by ESIF, reducing the scope for complementarity between different instruments and policy objectives – for instance, the provision of ESIF co-financed grant support to promote 'investment-ready' businesses could not be coupled with ESIF cofinanced business loans or equity under this model, potentially requiring different approaches to policy coordination.
- If the areas of intervention remained unchanged, ESIF and its cofinancing would become less sustainable since all funds would be non-repayable. This would arguably be a retrograde step in areas such as SME support where legacy funds have come to be seen as important advantages of repayable support.[183]
- The use of FIs in 2007-13 was perceived by many Managing Authorities to involve a shift away from a 'subsidy culture'; a large number of respondents noted that FIs had a positive impact on the competitiveness of financial recipients or were more likely to attract high quality applicants than grants, in this context returning to grant-only based support even for revenue-generating projects would be a step backwards.[184]

- e) Presumption in favour of FIs

A related but qualitatively different approach to encouraging the uptake of FIs would be to introduce ***a presumption in favour of financial instruments in support of revenue-generating projects***. Under this approach, support for potentially revenue-generating projects in the form of grants would need to be explicitly justified. In a sense, this would extend the use of ex ante assessments to grant interventions – there is perhaps already a mismatch in having an obligatory ex ante assessment to justify using

[181] See page 107.

[182] See page 76.

[183] See page 85.

[184] See page 88.

repayable forms of intervention, but no requirement to justify the use of *non*-repayable funds.

The main ***advantage*** of this approach is that it makes financial instruments the default policy delivery mechanism, unless otherwise justified. As under the ring-fencing option described above, this could force a more thorough and more imaginative consideration of where and how financial instruments could be used.

The key ***disadvantage*** of requiring a systematic justification for the use of grants is that it could simply become a 'tick box' exercise rather than entail a real consideration of repayable support options. An ex ante assessment for grant interventions is potentially a major exercise unless the scope were narrowed down and justification were only required for certain thematic objectives or priorities. Even so, it could be argued that encouraging the use of FIs might be better achieved through persuasion and presentation of successful examples than by requiring systematic justification for their non-use.

6.3.4. Final remarks on the options for increasing uptake of financial instruments

Some of the options outlined above represent quite radical and rather arbitrary approaches to future ESIF FI policy and they have been presented as if they were mutually exclusive.. However, the recommendations that emerged from the study emphasised the need for policy ***stability,*** and this would rule out some of the options outlined above, notably:

- Limiting ESIF spending to 'grants only'
- Limiting ESIF FI spending to using only off-the-shelf-models
- Limiting the use of ESIF FIs only to EU level instruments
- Ring-fencing a minimum amount within OPs for spending on FIs.

In practice, the most effective way forward is likely to lie in combining *elements* of these options, and taking a more nuanced approach that takes account of past experience. Such an approach is summarised for the two core options (Status Quo and Status Quo+) in Figure 6.3.

Figure 6.3: 'Finessing' the options

	OTS	EU level instruments	Presumption in favour of FIs
Status Quo	Increase the range of OTS options; extend flexibility – eg making more use of GBER	Enable use of EU level instruments as now, but review the role of EU level FIs and their interface with ESIF FIs, including assessment of funding needs under ex ante assessment.	Where grants are proposed for revenue-generating projects, explicit justification should be sought.
Status Quo plus	OTS options could be increased, but this may be less critical if State aid and procurement issues addressed	In the absence of major State aid and procurement issues for shared management FIs, the role of EU level FIs might shift and be more oriented towards OPs considered too small for FIs	Where grants are proposed for revenue-generating projects, explicit justification should be sought.

In essence, and in line with the recommendations for policy ***stability*** outlined above, this takes an incremental approach to policy change and supporting the uptake of FIs – building on policy experience, learning and the development of administrative capacity, but adjusting policy to maximise the benefits from elements that have or could work well. In the meantime, the simplifications included in the proposed 'Omnibus' Regulation have yet to be adopted, and the impact of these changes in terms of helping encourage greater uptake of FIs will only be seen over time. The use of co-financed FIs has involved the build-up of administrative capacity and of the policy networks needed to facilitate their use. Regulatory stability is essential to consolidate this experience and to enable the focus to shift away from ***procedural challenges*** to concentrate on the ***substantive change*** that FIs can induce. For this, more and better information is needed to enable a fine-grained analysis of which co-financed financial products work and why: concrete evidence of how and where FIs can be effective, and models of 'success', would provide compelling reasons to increase their uptake.

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KN-02-17-974-3A-N

Publications Office

doi: 10.2776/981010