House of Commons Library

BRIEFING PAPER
Number 08145, 14 February 2019

The European Investment Bank

By Philip Brien

Contents:

Contents

Summary

The European Investment Bank (EIB) was set up in 1958 under the terms of the Treaty of Rome.[1] Based in Luxembourg, it is the European Union's bank, lending to projects that contribute to growth and employment within Europe.

The EIB is owned and controlled by the EU member states, and 91% of its lending has gone to countries within the EU. However, it does also back projects that are outside the EU, so long as they are economically sound and in line with the Bank's policy goals.

The Bank leverages capital paid in by its members to raise money on international bond markets at low rates, and lends out this money to projects. It chooses the projects to lend to based on the priorities of the EU, with decisions taken by a Board of Directors nominated by the EU member states.

The UK has paid in €3.5 billion in capital to the EIB (16% of the total). Since the Bank's founding, projects in the UK have received €118 billion in loans, 8.5% of the total lent.[2]

There is considerable debate about how the UK will work with the EIB after it leaves the EU. The main points of contention surround the capital that the UK has paid into the Bank, what any ongoing relationship with the Bank would look like, whether projects in the UK will continue to receive loans, and whether the UK could create its own replacement for the Bank.

The European Investment Fund, an offshoot of the EIB partly owned by private financial institutions, supports small and medium-sized enterprises throughout Europe by providing risk financing (for example, by backing venture capital firms). Its funding of UK venture capital has slowed since the UK's vote to leave the EU, although potential replacements have been mooted by the UK Government.

1 Some dates and figures, EIB.org, retrieved 6 November 2017
2 Projects financed, EIB.org, retrieved 5 February 2019

1. The EIB's membership

The Statute of the EIB, in line with Article 308 of the Treaty on the Functioning of the European Union, defines its members as the EU member states.[3] These states jointly own and control the Bank: they provide the capital which the Bank leverages for its operations, and they nominate ministers to serve on the Bank's Board of Governors, which takes decisions on how the Bank operates.

Although countries which are not members of the EU do not have any ownership or control of the Bank, they can still receive loans from the Bank for projects that are in line with the Bank's public policy goals – indeed, as the below table shows, over its existence just over 9% of the total value of loans from the EIB has gone to countries outside the EU.

Total loans from the EIB, by region
1959-2018

	€ billions	% of total
European Union	1,254.0	90.4%
EFTA countries	4.8	0.3%
Enlargement Countries	40.9	2.9%
Eastern Europe, Southern Caucasus and Russia	10.5	0.8%
Mediterranean countries	34.4	2.5%
Africa, Caribbean, Pacific countries + OCT	20.3	1.5%
South Africa	3.2	0.2%
Asia and Latin America	18.8	1.4%
Total	**1,386.9**	

Note: OCT = overseas countries and territories
Source: EIB.org, retrieved 1 February 2019

[3] EIB statute, 1 July 2013, Article 3

2. How the EIB works

Although the EU member states have all provided capital for the EIB, it does not directly lend this money out to projects. Rather, it leverages its capital to borrow on international bond markets, using its very high credit rating[4] to borrow at good rates and then lends this money.

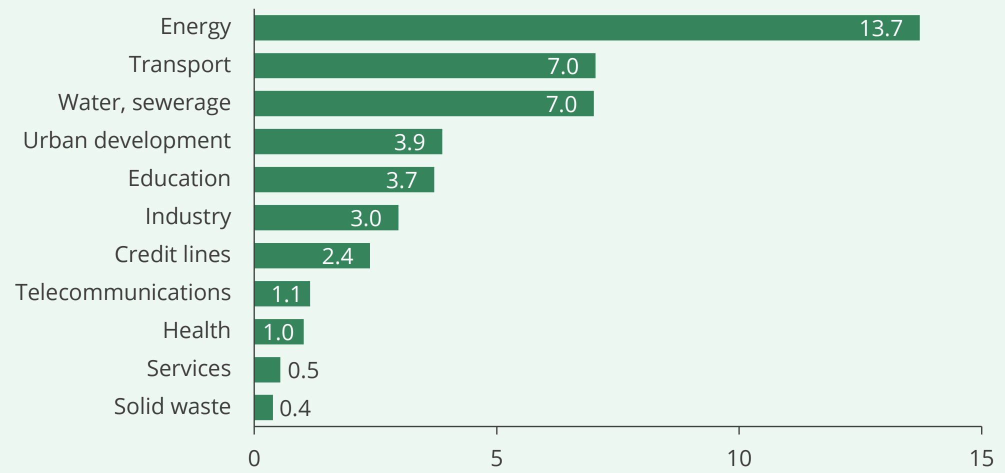
The Bank lends to projects that it thinks will further its policy goals. At present, these are:

- Innovation and skills
- Small and medium-sized enterprises
- Infrastructure
- Climate and environment

These links go to further details on each of these policy areas on the EIB's website.

The EIB publishes details on every project that it has financed. A sectoral breakdown of all the projects that it financed in the UK between 2010 and 2018 can be seen below.

EIB lending to the UK, by sector
€ billions, 2010-18



Source: EIB.org, retrieved 1 February 2019

This shows that energy projects made up the largest lending sector over this period, followed by transport and sewerage.

An up-to-date list of all the projects financed by the EIB in the UK between 2010 and 2018 can be found here.

Day-to-day decisions in the running of the Bank, including decisions on which projects should be funded, are taken by the Board of Directors. This Board is nominated by the member states and the European Commission – each state nominates one director, the Commission nominates one, and nineteen alternate directors are also nominated by

[4] The EIB has AAA-ratings with all three major rating companies.

different groupings of member states, with greater weight given to larger and richer states.[5] Greater weight is also given to wealthier countries by the voting mechanism, which states that normal decisions are made by "at least one third of the members entitled to vote representing at least 50% of the subscribed capital".[6]

Box 1: Funding example: Thames Tideway Tunnel

The largest project funded by the EIB in the UK in 2016 was a £700 million loan towards the Thames Tideway Tunnel, the largest infrastructure project ever undertaken by the UK water industry.[7] This project is intended to upgrade London's Victorian sewer system, to cope with the fact that its existing sewers currently overflow into the Thames on a weekly basis – when they were first constructed, this would happen only once or twice a year, during heavy storms. By building a 25 kilometre tunnel under and alongside the Thames, the sewage can be transported safely to Beckton Sewage Treatment Works, which will reduce pollution in the Thames.[8]

The entire project is projected to cost £4.2 billion and will take seven years to build across 24 different sites, with tunnelling starting in 2018. The EIB loan goes some way towards offsetting this cost, and will be drawn down in ten tranches and paid back over 35 years, at a variable interest rate linked to RPI inflation.[9]

5 For example, Germany, France, Italy and the UK each nominate two alternate directors; at the other end of the scale, Bulgaria, the Czech Republic, Croatia, Cyprus, Hungary, Malta, Poland, Slovenia and Slovakia nominate four alternate directors between themselves.

6 EIB statute, Article 10.

7 United Kingdom: GBP 700m EIB backing for Thames Tideway Tunnel, EIB.org, 12 May 2016

8 Our solution, Tideway, 17 July 2017

9 Debt summary – Q2 FY17/18, Tideway, 5 October 2017

3. Brexit issues

Several major issues related to the EIB have come about as a result of the UK's decision to leave the EU. Some are still under active negotiation, and are subject to change depending on the final outcome of the Brexit process. Some of the main issues are listed below.

3.1 The UK's capital contribution to the EIB

The UK has agreed to provide €39 billion of the EIB's capital, as per Article 4 of the EIB's statute. However, the statute also provides that only around 9% of this money had to be paid in immediately, with some or all of the remainder to be called in if the Bank's Board of Directors deems it necessary. This means that as of May 2018, the UK had contributed just under €3.5 billion.[10]

When the UK leaves the EU, under the current rules it would cease to be eligible to be a member of the EIB. Under the terms of the Withdrawal Agreement currently before Parliament, its capital contribution would therefore be returned, once all the EIB's outstanding loans at the time of the UK's withdrawal have concluded; this could take until 2054, according to Alexander Stubb, the EIB's vice president.[11]

The UK's €3.5 billion of paid-in capital will be repaid to the UK in twelve annual instalments starting at the end of 2019. Article 150(4) of the Withdrawal Agreement says that starting from 15 December 2019, the UK will receive eleven instalments of €300 million and a final instalment of €195.9 million. Should any liabilities be triggered, then the UK will still be liable for its share of the paid-in capital.

Article 150 sets out that the UK shall remain liable for financial operations approved by the EIB before the WA enters into force and explains how this liability will be managed in the future. The UK shall provide a guarantee to the EIB equal to its current callable capital – an amount the UK currently agrees to provide if required. This guarantee will decrease as EIB loans associated with it decrease. Article 150(6) sets out how any triggered liabilities will be dealt with.

3.2 No share of the EIB's profits

The Withdrawal Agreement also sets out that the return of the UK's capital represents the only payment that the UK will receive in respect of its membership of the EIB. In January 2019, a report from the House of Lords EU Financial Affairs Sub-Committee pointed out that the EIB has made a profit from its lending operations, and that a share of those profits in proportion to the UK's shareholdings would have come to approximately €7.6 billion, more than twice the UK's paid-in capital.

The report noted that there was no mention in the EIB's statute of how this profit should be handled in the event that a Member State left the

10 EIB 2017 Financial Report, table H.1.
11 Brexit: EU bank may not fully repay UK until 2054, *BBC News*, 27 October 2017

EU, but suggested that the Government had not pressed for it to be taken into account, and asked the Government to explain why.[12]

3.3 A continuing relationship with the EIB

Under EU law, the UK will cease to be a member of the EIB after Brexit. However, there have been suggestions that its relationship with the EIB could continue in some form. The Chancellor, Philip Hammond, suggested as much in his Mansion House speech on 20 June 2017:

> In the long-term, it may be mutually beneficial to maintain a relationship between the UK and the EIB after we leave the EU.
>
> And we will explore the options together.
>
> But we cannot take chances. So we will be prepared, in case we do not maintain that relationship.[13]

This position was echoed in the response to a question by Seema Malhotra MP on the UK's future relationship with the EIB on 5 September 2017, when David Davis said:

> So far, the negotiations have only been about the departure arrangements—what would happen in the event of a rift—but when we get to the point of talking about the ongoing relationship, I think we will be looking to maintain that ongoing relationship.[14]

Even following the conclusion of the Withdrawal Agreement, the Government has not made any statements on the exact form that such a relationship could take, although paragraph 15 of the Political Declaration on the future relationship between the UK and EU says that "the Parties note the United Kingdom's intention to explore options for a future relationship" with the EIB.[15]

In their report mentioned in the previous section, the House of Lords EU Financial Affairs Sub-Committee listed several options for the UKs future relationship with the EIB. The report noted that the UK could not remain fully part of the EIB without EU treaty changes, which seemed unlikely. Although it could still receive funding as a third country, this would probably result in lending to the UK being much lower than when it was a Member State; alternatives could include establishing a subsidiary of the EIB for UK lending, or having a replacement bank (see below) work closely in partnership with the EIB.

3.4 Access to loans

The EIB does provide loans to countries outside the EU, as shown in the table in section 1 of this briefing. This implies that the EIB could potentially continue to fund projects in the UK after Brexit.

---

12 House of Lords EU Financial Affairs Sub-Committee, *Brexit: The European Investment Bank*, HL Paper 269, 31 January 2019
13 Mansion House 2017: Speech by the Chancellor of the Exchequer, HM Treasury, 20 June 2017
14 HC Deb 5 September 2017 c63
15 Department for Exiting the European Union, Political Declaration setting out the framework for the future relationship between the European Union and the United Kingdom, 25 November 2018

However, EIB lending outside the EU is governed by a series of mandates from the European Union in support of EU development and cooperation policies in partner countries. As a result, any continued lending to the United Kingdom would have to be unanimously agreed by the EIB's board of governors (the finance ministers).

Because the vast majority of loans go to EU member states (and much of the remainder goes to the EFTA countries and countries that are seeking to join the EU), it seems likely that the UK would have access to significantly less funding than it does now, if it has access to any at all.

There have been some news reports (see, for example, The Times, European Investment Bank cuts off cash for British building projects due to Brexit, 22 August 2017) suggesting that the EIB has already decided not to make long-term loans to projects in the UK while the Brexit negotiations continue. The EIB's own data would seem to bear this out, showing that lending to the UK has decreased dramatically since 2016:

European Investment Bank loans to the UK, 1973-2018
€ billions, not adjusted for inflation

Source: EIB.org, retrieved 1 February 2019

Lending to the UK in 2018 was at its lowest level since 1984, even without taking inflation into account. Although some of this could be explained by the EIB performing greater due diligence on loan recipients, it is also possible that the terms required on loans since 2016 have made them much less attractive to UK borrowers.

In April 2018 the Financial Times reported that an internal report from the EIB commented on this decrease, saying that "The reason the volume has gone down is not because the UK is not any longer allowed to be the recipient of investments" and that the decrease "comes as much from a decrease in demand [in the UK] as well as complexity of concluding the operations and deals because we have to deal with issues we didn't have to deal with before because of the uncertainty from Brexit."[16]

3.5 Preparations for a no-deal Brexit

The Government's guidance about EIB financing in the event of a no-deal Brexit[17] points out that the *European Union (Withdrawal) Act 2018*

16 Financial Times, European Investment Bank pulls back on UK funding after Brexit, 20 April 2018

17 HM Treasury, European Investment Bank Group financing if there's no Brexit deal, 10 January 2019

protects the EIB's rights to finance projects in the UK.[18] Any loans which have already been agreed with the EIB will therefore continue even in a no-deal scenario.

3.6 A UK replacement for the EIB

In the event that the UK does not secure an ongoing relationship with the EIB, one of the ideas that has been floated is that the UK could set up its own replacement. This option is not unusual in other countries, and does have some support in this one; indeed, the Scottish Government has already made plans to set up a Scottish National Investment Bank.[19] The Government also has experience in setting up investment banks for specific purposes, such as the Green Investment Bank.[20]

However, Werner Hoyer, president of the EIB, has described setting up an equivalent to the EIB as an "enormous challenge", saying that "it would take at least a decade" to get such a bank to the requisite size; another expert suggested that the UK would require between £15 billion and £20 billion of capital.[21]

It is also possible that a UK infrastructure bank would have to comply with EU state aid rules as part of the UK's future relationship with the EU. This does not prevent such a bank from being set up (the German national promotional bank KfW is compliant with the rules), but it would be an extra complication.[22]

The Government has steered clear of suggesting a UK replacement for the EIB so far. The Chancellor stopped short of suggesting it as a possibility in his Mansion House speech in June 2017, stating only that he was "expanding the support available to capital funding in the UK".[23]

3.7 The EIB's future without the UK

The impact of Brexit will not only be felt in the UK – it will also necessitate changes for the EIB. This is because many of the EIB's own rules (such as those on voting rights or the size of the Bank's reserve fund) are based heavily on the level of the Bank's subscribed capital. Crucially, Article 16 of the Bank's Statute says that the Bank can only lend up to 2.5 times its total subscribed capital at any given time;[24] this means that the UK's withdrawal of its capital leaves a large hole in the Bank's lending capabilities.

---

[18] See section 4, European Union (Withdrawal) Act 2018

[19] Scottish Government, Scottish National Investment Bank: implementation plan, 28 February 2018

[20] For more details, see the Library briefing on Green Investment Bank: Proposed Sale, 24 January 2017

[21] Financial Times, UK infrastructure bank would face hurdles, say experts, 22 October 2017

[22] House of Lords EU Financial Affairs Sub-Committee, *Brexit: The European Investment Bank*, HL Paper 269, paragraphs 120-126, 31 January 2019

[23] Mansion House 2017: Speech by the Chancellor of the Exchequer, HM Treasury, 20 June 2017

[24] EIB Statute, Article 16

The EIB has therefore begun to look at ways of coping with the UK's exit, such as increasing the amount of capital that the remaining shareholders contribute. However, a number of EU Member State governments have insisted that changes of this kind should also be linked to the Bank's willingness to reform, particularly in reference to its management and oversight.[25]

Poland's government, on the other hand, has argued that the UK's capital should be replaced – specifically, they want to increase their own contribution and thereby increase their own representation in the way that the EIB is run. Germany, meanwhile, wants the European Central Bank to have a greater role in oversight, in order to reduce the level of risk in the projects it chooses. These arguments are likely to continue for some time after the UK has left.[26]

---

25 Financial Times, European Investment Bank faces call for overhaul after UK exits, 18 July 2018

26 Financial Times, The fight for the future of the EIB, 17 September 2018

4. The European Investment Fund

Founded in 1994, the European Investment Fund (EIF) provides investment and loans targeted specifically at small and medium enterprises (SMEs) in Europe. It is controlled by the EIB, the European Commission, and financial institutions from the EU member states.

In 2017, the EIF signed transactions totalling €9.3 billion, supporting funds such as venture capitalists and angel investors. This is expected to leverage over €35 billion of funding for businesses in Europe.[27]

Since the UK's vote to leave the European Union, EIF funding of UK venture capital firms has markedly slowed. The EIF said immediately after the vote that it would "not change its approach to operations in the UK," and indeed it states that lending to UK projects will continue. However, because of the potential impact of Brexit, it now also says that "due diligence on them now needs to be more thorough, and take into account a wider range of factors."[28]

The Chancellor announced measures to help the UK's venture capital industry in November 2016, by making an additional £400 million available to the British Business Bank, a government-owned development bank which backs venture capital firms.[29] In August 2017, this was followed up by the launch of a consultation on setting up a National Investment Fund to replace the EIF.[30] The consultation, Financing growth in innovative firms, closed in September 2017; in October 2018, the Government published an update (Financing growth in innovative firms: one-year on). This update said that:

- "the British Business Bank has the capacity this financial year to make venture capital commitments that would exceed the combined average annual commitments from the European Investment Fund and British Business Bank in the years preceding the UK's vote to leave the EU";
- "at Budget 2018 the Chancellor announced that if no future relationship with the European Investment Bank Group is in place before the UK leaves the EU on 29 March 2019, the government will provide the British Business Bank with the resources to enable it to make up to £200 million of additional investment in UK venture capital and growth finance in 2019-20."

27 EIF Annual Report 2017, EIF.org, 25 April 2017
28 Financial Times, UK tech investors face loss of significant funding after Brexit, 10 May 2017
29 Chancellor announces additional £400m for British Business Bank to support innovative scale-up businesses, British Business Bank, 23 November 2016
30 New National Investment Fund to back innovative UK firms, gov.uk, 1 August 2017

5. Further reading

The Library has produced some other work on the EIB:

- Brexit: future funding from the European Investment Bank? (blog entry, November 2016)
- Library briefing paper UK Funding from the EU (November 2018), sections 5 and 7.3

The EU has also produced some useful material:

- European Parliament: EIB factsheet (June 2017)
- European Parliamentary Research Service: The €315 Billion Investment Plan For Europe (December 2014)

BRIEFING PAPER
Number 08145
14 February 2019