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CEEP response to the consultation on the Europe 2020 Project Bond Initiative

CEEP (European Centre of Employers and Enterprises providing Public Services) welcomes the Commission's consultation on the 'EU 2020 Project Bond Initiative'. Given the financial challenges facing member states and the gap in financing large infrastructure projects this consultation is both timely and critical for improving future infrastructure funding. We are pleased to set out our responses to the general and specific questions below.

General questions

1. Is the chosen mechanism likely to attract private sector institutional investors to the sectors of transport, energy and ICT in particular?

The Commission's initiative to encourage infrastructure investment is welcome. Broadening the range of financing initiatives should help it to fulfil its objectives for bridging the gap between EU 2020 ambitions and budgetary realities. However, although project bonds can be a valuable tool in providing increased investment for the sectors outlined above, they are not an end in themselves, nor should they be allowed to hamper the normal recovery of capital markets in relation to the financing of infrastructure projects. In our view project bonds should complement existing sources of finance such as bank loans and grants.

We agree that including certain infrastructure projects already under construction, as suggested in the consultation, is in principle useful, because investment spending is particularly sensitive to budgetary pressures. We also agree that there is a track record of this type of project finance model for transport, and therefore, this area may readily lend itself to this type of financing. Also, there may be positive benefits for IT projects, particularly in the non-profitable areas of investments.

However, we are less convinced that issuing project bonds will incentivise investors in the energy sector where the costs of new technologies and timescales are untested. The consultation does not set out how project bonds will help address these challenges, if at all.

In addition, we know that historically the project bond market has a limited appetite for construction risk over long maturity periods. In our view and given the latter constraints, it will be important to inject some realism in to what can and what cannot be achieved through the issue of project bonds.

Finally, a primary issue is the sharing of financial risks, opportunities and burdens between the various parties, in particular private and public. The consultation remains largely vague on the relevant principles and instruments. Another important point in this context is the exact risk sharing between the EU and Member States' budgets on the one hand and the EIB or national investment/ development banks on the other. The relative roles would suggest that the former provide primarily investment grants while the latter provide loans or guarantees. There are also issues in relation to the suggested distribution of organisational and control responsibilities.

2. Are there other sectors with large-scale infrastructure financing needs that should be included?

We recognise the significance and scale of infrastructure investment needed in the next decade as highlighted in the EU 2020 strategy for transport, energy and communications. However, we believe that other sectors would also benefit from project bonds such as the health sector, urban development, education and the social sectors. PPP/PFI projects have been prevalent in a number of countries across a diverse range of sectors, thus the Commission should consider broadening the sectors for this type of infrastructure investment.

Specific questions

3. Would the credit enhancement facilitate/accelerate the conclusion of financing packages?

In our view the proposed 'credit enhancement' which would result in a new class of project bond being issued has the potential to attract investors. However, given that the declared reference model for this proposal is the 'Loan Guarantee Instrument' already used by the EU/EIB for financing trans-European transport projects, we believe that the experience gained with this instrument should be made public and included into the consultation debate.

4. What minimum rating of the bonds would be sufficient to attract investors? –

5. What degree of credit enhancement would be necessary to achieve this rating? --

6. Which impact would the Initiative have on financing costs and on maturities?

The proposal for a new class of project bond to reduce funding costs over longer maturity periods is a welcome initiative, particularly in a financially constrained environment where the maturity periods of bonds have generally been shortened.¹ Historically, the issue of project bonds has proven to offer investors longer-term financing, however, it still remains uncertain as to whether the proposals set out in the consultation will be sufficient to attract new long term investment.

As well as considering financing costs and maturities we think that organisational measures also should be taken into account, including promoting a rapid transfer of expertise to financial markets. This may well help to overcome potential practical impediments in market take-up of bonds.

7. Is it essential that a single entity acts as controlling creditor?

Given the EIB's long-standing experience in the financing of infrastructure projects on LGTT, it would seem sensible that the EIB should act as the sole controlling creditor according to principles to be established in agreement with market participants.

¹ According to Latham &Watkins '*both bond investors and banks have shortened their maturities... settling in an 8 to 13 year period* (see Latham & Watkins, Client Alert, *Why project bonds now?*, August 2009).