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Brexit: the European Investment Bank

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The European Union Committee

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Q in footnotes refers to a question in oral evidence.

SUMMARY

The European Investment Bank (EIB) has been active in the UK since 1973, during which time it has lent more than €118 billion to key infrastructure projects. This has included funding for major energy projects, transport, water and sewerage, higher education and housing. In 2015 alone, the EIB provided £5.6 billion for 40 different projects, amounting to approximately one-third of total investment in UK infrastructure. The European Investment Fund (EIF), of which the EIB is the majority shareholder, has also played an important role in providing and supporting access to finance for UK SMEs through a variety of intermediaries.

Brexit means that the UK will no longer be a member of the EIB. The EU Treaties restrict EIB membership to EU Member States, meaning that any future cooperation with the EIB will almost certainly be on the basis of the UK being a third country. Despite this, the Government has said almost nothing about how it envisages that such a relationship would work. This is all the more worrying given the 87 percent fall in EIB funding since 2016 and the fact that new UK projects will no longer have access to the EIB after 29 March 2019, until and unless a future relationship is agreed. It is therefore seriously concerning that, with Brexit and the associated loss of access to EIB financing a matter of weeks away, the Government has said nothing publicly about its ambitions for a future relationship with the EIB.

Under the Withdrawal Agreement, the UK will, over a period of 12 years, receive the €3.5 billion of capital it has paid in to the EIB. However, the UK will not receive any share of the profits that the EIB has accumulated, nor any interest or dividends. Given that this could amount to €7.6 billion, almost 20 percent of the UK's obligations under the £35–39 billion financial settlement, we regret that the Government has failed to provide an adequate explanation of the position taken in the negotiations.

Losing access to the EIB will have negative consequences for the financing of UK infrastructure. Not only does the EIB offer cheaper and longer-term loans than commercial lenders, but the quality of its independent expertise and due diligence also provides projects with a stamp of approval that crowds in additional private investment. While the Government has taken some steps to alleviate potential difficulties for SMEs, notably through additional resources for the British Business Bank (BBB), more remains to be done. Riskier infrastructure projects and those falling within the EIB's broader social mandate may find it more difficult to access alternative sources of finance at similar cost.

Given the vital role of infrastructure investment, the Government should consult on establishing a UK infrastructure bank, in line with the recommendations of the National Infrastructure Commission. We call on the Government to explore this option within its infrastructure finance review and, depending on the outcome of that review, to launch a consultation on the possible design features of a UK infrastructure bank as part of its upcoming National Infrastructure Strategy. As the UK loses access to the EIB, this would be an important step in supporting the financing of key infrastructure after Brexit and into the future.

Brexit: the European Investment Bank

CHAPTER 1: INTRODUCTION

Brexit: the European Investment Bank

1. Brexit means that the UK will no longer be a member of the European Investment Bank (EIB). This report considers the role of the EIB in the UK and options for the future relationship after Brexit, as well as domestic replacements such as the creation of a UK infrastructure bank. It begins in Chapter 2 with an overview of the EIB's structure and activities in the UK, examining the unique features that enable it to play an important role in supporting investment across a range of sectors.

2. Chapter 3 assesses the impact of Brexit on the EIB's lending to the UK since the referendum. It also examines the return of the UK's share of the paid-in capital of the EIB and options for any future relationship, given that the Government has yet to specify its preferred model. Chapter 4 moves on to the consequences of losing access to EIB funding and the extent to which this could be replaced by the private sector. It considers both large-scale infrastructure projects and funding targeted at SMEs, the latter of which currently falls within the remit of the British Business Bank.

3. Finally, Chapter 5 reviews recent arguments in favour of establishing a UK infrastructure bank to replace lost funding from the EIB. The chapter also considers possible barriers to doing so, such as EU State aid rules and measurements of public sector debt, as well as considerations relevant to the design of such an institution.

4. The EU Financial Affairs Sub-Committee, whose members are listed in Appendix 1, commenced the inquiry in July 2017. We received a number of written submissions and held oral evidence sessions with seven panels of witnesses during September, October and November 2018. We are grateful to all our witnesses.

5. **We make this report to the House for debate.**

CHAPTER 2: THE EIB AND ITS ACTIVITIES IN THE UK

The EIB and its mandate

6. The European Investment Bank, founded in 1958, is the world's largest multilateral borrower and lender by volume, aiming to provide finance and expertise for sound and sustainable investment projects which contribute to furthering European Union policy objectives. The European Investment Bank Group, formed in 2000, comprises the European Investment Bank (EIB) and the European Investment Fund (EIF).

7. The EIB is principally focused on four key priorities: infrastructure; climate and environment; innovation and skills; and small and medium-sized enterprises (SMEs), the last primarily the focus of the EIF. The EIF was established in 1994, with a central mission of supporting Europe's micro businesses and SMEs by helping them to access finance. The EIF designs and develops venture and growth capital, guarantee schemes and microfinance instruments which specifically target this market segment. In this role, the EIF fosters EU objectives in support of innovation, research and development, entrepreneurship, growth, and employment. (See Box 1.)

Box 1: The European Investment Fund (EIF)

Whereas the EIB is wholly owned by Member States, the EIF is a public-private partnership. The EIB is the majority shareholder (with 62 percent of the shares) and it is also part-owned by the EU, represented by the Commission. Private financial institutions own 11.8 percent of the Fund. Rather than investing in companies directly, the EIF's activity is channelled through European venture capital and private equity funds. It invests both in funds with pan-European mandates and in funds with a country-specific mandate (including in the UK). While the EIB's SME and mid-cap activity[1] is typically focused on delivering financial support to established enterprises, mostly in the growth or maturity stages, the EIF concentrates on supporting enterprises in earlier stages of growth and the provision of guarantee schemes.

8. The EIB's mandate is set out in the EU Treaties and its Statute. All EU Member States are members of the EIB by virtue of Article 308 of the Treaty on the Functioning of the European Union (TFEU) and can be recipients of EIB loans. However, the EIB can lend to third countries for development purposes.[2] In 2017, approximately 10 percent of the EIB's lending was to around 150 "partner countries" (in southern and eastern Europe, the Mediterranean region, Africa, Asia, Latin America, the Caribbean and the Pacific). It works in these countries to implement the financial pillar of the EU's external cooperation and development policies by encouraging private sector development, infrastructure development, security of energy supply and environmental sustainability.

1 The EIB defines SMEs as those firms with 10–249 employees and mid-caps as those with 250–3,000.

2 Treaty on the Functioning of the European Union, OJ C 326 (consolidated version of 26 October 2012) Protocol (No 5) on the Statute of the European Investment Bank, specifically authorises the EIB, within the framework of the task set out in Article 309 TFEU, to grant financing for investment carried out, in whole or in part, outside the territories of the Member States. Article 209 TFEU, in conjunction with Article 208 TFEU, provides that the EIB "shall contribute, under the terms laid down in its Statute, to the implementation of the measures" that are "necessary for the implementation of development cooperation policy."

9. Article 212 TFEU provides that the EU "shall carry out economic, financial and technical cooperation measures, including assistance, in particular financial assistance, with third countries other than developing countries".[3] Such measures are to be consistent with the development policy of the EU and are to be carried out within the framework of the principles and objectives of the EU's external action.

The EIB's lending in the UK

10. The EIB has been working with the UK since its accession in 1973. Over this time, it has lent more than €118 billion in the UK across different sectors of the economy, notably in the areas of energy, transport, water and housing. The volume of this funding has gradually increased over time, with 70 percent (€83 billion) of EIB funding being provided in the last 20 years and 45 percent (€53 billion) since the financial crisis.[4] In 2015 alone, the EIB provided £5.6 billion for 40 different projects in the UK, amounting to approximately one third of total funding of UK infrastructure.[5]

11. More than one-quarter of the EIB's financing for the UK has gone to the energy sector. The EIB's activities in this area are governed by its strict energy lending criteria, to ensure that the projects it supports adequately reflect the EU's energy and climate policies. The EIB has also pioneered the use of 'green bonds' to help finance its renewable energy and energy efficiency lending, having issued to the world's first Climate Awareness Bond (CAB) in 2007.[6]

12. As a result, much of the EIB's support for the UK energy sector has gone towards promoting sustainable sources of energy. This has included providing over €3 billion for developing and expanding the UK's offshore wind industry, which has now become a sophisticated market for energy investment. One example of this support was the £525 million loan granted to support construction of the Beatrice windfarm off the Caithness coast in north-east Scotland. When completed, this will generate enough electricity to meet the energy needs of more than 475,000 homes.[7]

13. The success of the UK's offshore wind industry is often cited as an example of the EIB's active involvement in effectively 'de-risking' these projects and encouraging investment from the private sector. It has been able to do this thanks to the public guarantee it has from the EU's Member States,[8] as well

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3 Article 212, Treaty on the Functioning of the European Union

4 European Investment Bank, 'Finance projects: multi-criteria list': http://www.eib.org/en/projects/loan/list/index.htm [accessed 10 December 2018]

5 European Investment Bank, Press Release, *EIB confirms GBP 5.6 billion record UK lending* (14 January 2016): http://www.eib.org/en/infocentre/press/releases/all/2016/2016-005-european-investment-bank-confirms-gbp-5-6-billion-record-uk-lending.htm [accessed 25 January 2019]

6 European Investment Bank, Press Release: *10th anniversary of "green bonds" celebrated in Luxembourg* (5 July 2017): http://www.eib.org/en/infocentre/press/releases/all/2017/2017–184-10eme-anniversaire-des-emissions-vertes-celebre-au-luxembourg.htm [accessed 18 December 2018]

7 European Investment Bank, Press Release, *GBP 525m European backing for Beatrice windfarm off Caithness coast* (23 May 2016): http://www.eib.org/en/infocentre/press/releases/all/2016/2016–121-gbp-500m-european-backing-for-beatrice-windfarm-off-caithness-coast [accessed 18 December 2018]

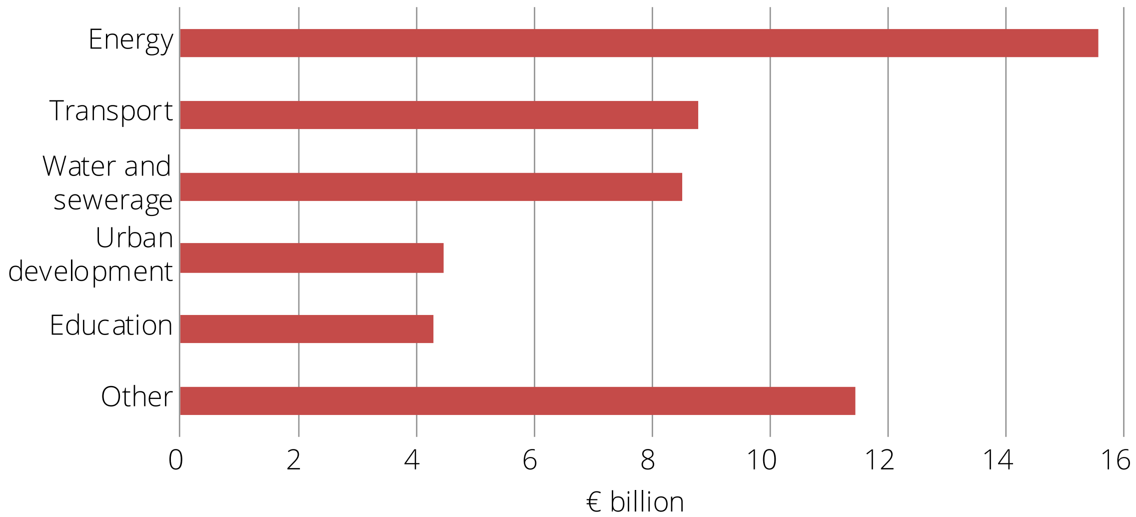
8 The EIB has €21.7 billion of paid-in capital as well as €221 billion of subscribed callable capital, which Member States have a legal obligation to pay if required.

as the returns it has generated from previous projects. Peter Clutton-Brock, a researcher at the climate and environment think tank E3G, told us:

> "There is no shortage of capital in the capital markets to fund energy assets. However, the types of technologies that are being developed often come with a new technology risk for some institutional investors and some mainstream public project finance investors, so the ability of the EIB to take on some of the project risk and technology risk is a major contributing factor. They would not be there without it."[9]

14. The EIB has played an important role in supporting some of the UK's most significant transport infrastructure projects in recent years, providing almost €8.8 billion of financing over the last decade. Speaking on behalf of Transport for London (TfL), Alex Conway, Assistant Director for Brexit and European Programmes at the Greater London Authority, noted that the EIB had been a "very important partner" in Crossrail, London Overground, and the Tube and Docklands Light Railway extensions. It has also provided £600 million for major road transport routes in Scotland, helped introduce new trains on the East Coast Main Line, supported the expansion of Greater Manchester's Metrolink network, and provided £825 million of funding for ports and harbours across the UK.

Figure 1: Volume of UK projects supported by the EIB since 2008



Source: European Investment Bank

15. Across Europe transport has been the sector that has received the most EIB support since the bank's foundation in 1958. It has benefited from the EIB's public mandate, in this case regarding the flexibility of its contracts. Speaking about the EIB's £1 billion loan for the construction of Crossrail in south-east England, which will ultimately increase London's rail capacity by 10 percent, Alex Conway told us:

> "One of the important things for Crossrail was that the EIB facility allowed the interest rate and the start date of a loan to be agreed well ahead of the required drawdown, which is not an option available when

9 Q 20

borrowing from … capital markets. That really helps to manage interest rate risk and the funding risk."[10]

16. The EIB has also been an important provider of finance to the UK's water and sewerage systems. In 2015 it provided a £530 million loan to support Severn Trent's investment programme for drinking water and waste water treatment. The EIB also backed the Thames Tideway Tunnel in 2016 with a £700 million loan, in what has been the largest infrastructure project ever undertaken by the UK water industry. Often dubbed the 'super sewer', the project is urgently needed to help tackle overflows of untreated sewage into the river as it flows through the centre of London.

17. The EIB has likewise played an important role in supporting urban development in the UK, notably in the housing sector. Under its mandate, the EIB cannot lend to property construction schemes unless they have a social element, and this has predominantly occurred in the area of social housing. For example, in recent years it has provided £1.5 billion to the Affordable Housing Finance programme in partnership with The Housing Finance Corporation (THFC), which will support the construction of 20,000 new affordable homes in areas of Glasgow, Wigan, Scarborough, Bradford and Cambridge. Since 2014 it has worked directly with large housing associations such as Sanctuary as well as local government. Just before the EU referendum, in June 2016, the EIB announced £280 million of support for two major social housing projects in Northern Ireland.

18. Unite the Union, the largest trade union in the construction sector, which has a significant number of members in the UK social housing sector, believed that losing access to EIB funding "could stymie affordable housing development".[11] In a similar vein, the East of England European Partnership told us: "As with local authority areas across the UK, the need for more housing is acute and the removal of another option by which to finance new building stock without a replacement will be a blow to local authorities post-Brexit."[12]

19. Higher education has also increasingly benefited from access to the EIB, which since 2010 has provided more than £2.1 billion in loans to thirty universities across the UK. This funding has mainly been used to fund campus development, including the construction, redevelopment and refurbishment of campus facilities (such as libraries, sports facilities and science parks), the expansion or upgrading of research and teaching facilities, and the funding of new academic buildings and student residences. While some universities have recently been able to secure financing from private bond markets, these are more expensive and only available to those universities with the highest credit rating.[13]

20. Mark Drakeford AM, the then Cabinet Secretary for Finance in the Welsh Government, told us that the EIB has provided "substantial sums of capital" for investment in campus developments at Swansea and Bangor universities.[14] Philip Harding, Director of Finance and Business Affairs at University College London (UCL)—which in 2016 received £280 million from the

10 Q 24
11 Written evidence from Unite the Union (EIB0012)
12 Written evidence from the East of England European Partnership (EIB0006)
13 Q 20
14 Written evidence from the Welsh Government (EIB0004)

EIB to upgrade and expand its Bloomsbury campus in central London, as well as for the building of UCL East, the university's new site at the Queen Elizabeth Olympic Park in east London—underlined the EIB's importance for the higher education sector:

> "As to the nature of university investments, particularly large-scale infrastructure investments, universities are charities; they are not-for-profit organisations. Typically, these sorts of projects do not pay back very quickly, nor do they generate particularly attractive financial returns. Often, the benefits are secured over a longer period and are largely intangible or difficult to quantify; they enhance the value that students get from their experience by being able to access high-quality facilities and improve the quality and quantity of research output from universities."[15]

21. Other significant areas of EIB support include the financing of research and development projects in sectors such as aircraft manufacturing and pharmaceuticals, the expansion of 3G/4G mobile networks across the UK, and the construction of new hospital buildings, including in Birmingham and Liverpool. The EIB has also provided almost €3.9 billion in subsidised credit lines to commercial banks to improve their provision of SME finance, as well as regional public investment vehicles such as the Northern Powerhouse Investment Fund, the Midlands Engine Investment Fund and the North East Fund.

22. In addition, the EIF has played an important role in facilitating access to finance for SMEs and mid-caps. Operating through financial intermediaries, it indirectly supports investment into some of the most high-potential and innovative small companies in the UK. The British Private Equity and Venture Capital Association (BVCA) told us that the EIF had been a significant player in the UK and European venture capital market: "Between 2011 and 2015, the European Investment Fund invested €2.3 billion into UK venture capital, growth and mid-market funds, which in turn supported total investment of €13.8 billion into SMEs."[16] This meant that about 37 percent of venture capital raised in the UK over this period came from the EIF.[17]

23. **The EIB has been an important provider of funding for the UK, including almost €50 billion over the last decade. This has included the financing of key projects in areas such as energy and the environment, transport, water and sewerage, education and housing. The EIF has also been an important investor in UK venture capital, growth and mid-market funds, facilitating access to finance for SMEs. As the UK will lose access to these important sources of finance, there will be negative consequences for future projects in these areas unless alternative sources are established.**

How the EIB supports investment

Provision of cheaper, long-term financing

24. As a result of its public guarantee, and its track record of successfully supporting projects across Europe, the EIB has been granted a AAA credit

15 Q 20
16 Written evidence from the British Private Equity and Venture Capital Association (EIB0009)
17 Q 46

rating by all of the major credit rating agencies, enabling it to borrow cheaply on capital markets. Combined with the fact that the EIB is not required to operate on a profit-making basis, this means that it can provide finance for projects more cheaply than commercial lenders. Its focus on long-term finance also allows it to fill a gap that may otherwise be left unfilled by the private sector. Robert Jenrick MP, Exchequer Secretary to the Treasury, told us that "there are specific advantages where the EIB has proven itself in offering loans of long duration, which are important to particular infrastructure projects".[18]

25. The benefits of the EIB's ability to provide cheaper, longer-term financing were underlined in much of the evidence. The Infrastructure Forum, which brings together investors in and builders and operators of UK national infrastructure—and which established a specific working group in 2017 to examine the significance of and future options concerning EIB lending in the UK—noted that the EIB provided funding at a lower cost than the capital markets: "This subsidised lending enables infrastructure projects in the UK to be delivered more cheaply than they could be otherwise."[19]

26. The Infrastructure Forum also explained that there were advantages to the EIB's appetite for supporting long-term investments, which could reduce the risk of refinancing before a project has been completed. It can often provide longer-term loans compared to the private sector, within financing periods that can be as long as 30 years. If access to the EIB is lost as a result of Brexit, it stated, "This long termism may be difficult to replace."[20]

27. The value of the EIB's cheaper and longer-term financing was also recognised by local authorities and devolved administrations. The East of England European Partnership explained that the availability of assured, long-term finance at competitive rates had been one of the "key factors in organisations in the East of England obtaining finance from the EIB alongside a range of other sources".[21] Mark Drakeford AM also noted that the EIB provided long-term, low-cost capital for necessary investment in public and private infrastructure. He warned about the possible consequences of losing access to the EIB post-Brexit:

> "The effective withdrawal of EIB finance has a quantifiable cost. An increase of 200 basis points in the cost of capital would lead to an increase in costs of around £1.5 million per annum for each £500 million borrowed. The additional financing costs caused by higher interest rates would lead to a significant loss of productive investment in Wales and across the whole of the UK."[22]

28. James Richardson, Chief Economist at the National Infrastructure Commission (NIC)—established in 2015 to provide the Government with expert advice on the UK's long-term infrastructure needs—referred to the UK's offshore wind industry, telling us that the EIB's role had been "key in bringing down the price and making it much more viable to deploy these

18 Q 77
19 Written evidence from The Infrastructure Forum (EIB0007)
20 *Ibid.*
21 Written evidence from the East of England European Partnership (EIB0006)
22 Written evidence from the Welsh Government (EIB0004)

renewables at scale in a cost-competitive way".[23] Peter Clutton-Brock, from E3G, agreed:

> "It is the fact that the EIB has an AAA rating and is therefore able to borrow relatively cheaply from the capital markets, coupled with the fact that it does not have a mandate requiring it to achieve a commercial return, which allows it to offer slightly cheaper finance than other private institutions."[24]

29. The same applied to the transport sector. Speaking on behalf of TfL, Alex Conway told us that "the main value is that [the EIB] is the lowest-cost form of finance". Current EIB loans to TfL are worth about £3.3 billion—around 30 percent of its direct borrowing—and have resulted in "significant savings compared with TfL's other long-term funding options". Mr Conway warned about the effect of losing access to the EIB: "With future important investments of the likes of Crossrail 2, that might increase the price, which might have an effect on the ultimate viability of the scheme. There is genuine concern."[25]

30. Piers Williamson, Chief Executive at The Housing Finance Corporation (THFC), characterised the EIB's financing for housing development as a form of subsidy: "In my market, it is cheap funding; it is the cheapest long-term funding that one can get."[26] Moreover, this lower cost form of finance "can be used almost as an accelerant; phases of regeneration that might not happen can be encouraged to happen because, essentially, it provides a revenue subsidy over commercial forms of funding."[27]

31. Witnesses from the higher education sector told us that the EIB provided one of the few opportunities to secure long-term, attractively priced finance, and stressed in particular the importance of the EIB's long time horizon. Universities UK told us about the lack of long-term certainty in commercial loans and argued that investment in campus developments "cannot take place without long-term commitment".[28] Philip Harding from UCL told us:

> "Prior to [working with the EIB], the primary source of debt finance for universities was bank lending, at the time when banks were prepared to lend long term and at attractive rates to universities. That is no longer the case. Typically, bank lending for universities is now limited to much shorter periods of between five and seven years … The EIB offers one of the few opportunities to secure long-term, attractively priced finance. In our case, the finance was over a 30 year term."[29]

32. The EIF also has a AAA credit rating, and is able to offer longer-term investment than is often provided by the private sector. Catherine Lewis La Torre, Chief Executive of BBB Patient Capital Holdings at the British Business Bank—the UK institution responsible for improving SMEs' access to finance—told us that the provision of long-term capital "is an obvious place where the EIF has played" a role.[30] The EIF also manages several

23 Q 6
24 Q 20
25 Q 28
26 Q 27
27 Q 20
28 Written evidence from Universities UK (EIB0008)
29 Q 20
30 Q 62

initiatives that aim to enhance access to finance for SMEs and small mid-caps where it shares some of the risk borne by financial intermediaries, which in turn can ultimately reduce the cost of borrowing.[31]

33. **The availability of cheaper, long-term financing from the EIB is one of its key benefits. Losing access to the EIB would almost certainly increase the cost of capital in different sectors of the UK economy and could mean that some future projects would no longer be commercially viable. Similarly, if the EIF withdraws from the UK market, small businesses may find it more difficult to access affordable finance. If access to the EIB and EIF is lost as a result of Brexit, the Government will need to ensure that comparable funding continues to be available.**

Independent expertise and due diligence

34. Many of our witnesses cited the importance of the EIB's independent expertise and due diligence for crowding in private investment, in addition to its cheap and longer-term financing.[32] This is an explicit objective of the EIB, which states: "The combined expertise of our economists, engineers, financial analysts and climate specialists ensures the success of our projects. In turn, the stamp of approval from our specialists triggers more investment from the private sector."[33] Philip Duffy, Director for Growth and Enterprise at HM Treasury, highlighted the importance of "the confidence it gives the overall market, because it has a very good due diligence process".[34]

35. The EIB's ability to conduct effective due diligence is a reflection of its large in-house expertise: it has 3,000 full-time staff including finance professionals, engineers, economists and environmental experts. They are responsible for comprehensively reviewing all projects that the EIB is involved with. Laurie Macfarlane, Public Banking Lead at UCL's Institute for Innovation and Public Purpose (IIPP), told us that one of the main benefits of the EIB was its breadth of professional expertise compared to private financial firms:

> "The EIB also employs significant engineering or scientific expertise that provides a broader way to assess projects, looking not just at prices and market signals but at fundamentals. That is quite important for its ability to crowd in private sector investment. If the EIB is a first-mover investor in something, it gives other investors the confidence to say, 'The EIB has looked at this and appraised it robustly using its wide range of expertise'. It gives them confidence to come in and invest."[35]

36. Organisations that work directly with the EIB made similar points. The Infrastructure Forum told us that many of the organisations within its network had praised the EIB's due diligence. It noted that, as a AAA-rated lender, the EIB's presence reassured investors. This effect was particularly

31 European Investment Fund, *We support innovators, entrpreneurs and social change makers across Europe* (13 October 2016): http://www.eif.org/news_centre/publications/fei_brochure_new.pdf [accessed 18 December 2018]

32 'Crowding in' describes the increased propensity of the private sector to invest as a result of an initial financial commitment from another party.

33 European Investment Bank, *EIB at a glance* (March 2018): http://www.eib.org/attachments/general/the_eib_at_a_glance_en.pdf [accessed 18 December 2018]

34 Q 80

35 Q 31

acute on large syndications, where the EIB could lead negotiations with experienced teams.[36]

37. Peter Clutton-Brock focused on the energy sector, noting UK investors were much more confident about investing in energy projects where the EIB had already applied its expertise and conducted due diligence: "Often more so than the cost of capital, that is a key factor in crowding in additional sources of finance".[37] Mark Drakeford AM underlined the importance of the EIB's expertise to the Welsh Government:

> "It brings a significant additional benefit for project promoters in the form of commercial expertise. The South Wales Metro project, for example, has benefited from the bank's commercial expertise to inform the procurement process, while previous investments in Wales have, similarly, benefited from expertise and best practice offered by the EIB."[38]

38. The EIB's expertise and due diligence was also recognised by the NIC. James Richardson told us that with the EIB "you have an established institution and the expertise, and people in the markets understand what it means if the EIB is willing to co-invest".[39] The Minister, Robert Jenrick MP, noted:

> "There are a number of areas where the EIB has particular expertise … it has maturity and a well-respected track record, and it has capacity, particularly in some areas of technology, such as renewables. It has a track record of supporting new technologies sooner than some other institutions; on wind power, for example."[40]

39. Independent expertise and due diligence are also key attributes of the EIF. From the FinTech industry, Victoria Roberts, Head of Government Affairs and Policy at Innovate Finance, focused on the EIF's advice and technical expertise, which underpinned its strong track record.[41] Tim Hames, Director General of the British Private Equity and Venture Capital Association (BVCA), also underlined the benefits of the EIF's comprehensive due diligence process:

> "The great thing about the EIF, although if you are a fund manager it could be a bit of a pain, is that it has a reputation for conducting due diligence, which at minimum is intense and at worst intrusive. Because it is European taxpayers' money, nobody goes over an applicant like the EIF does. It is a full-blown body search. If you are a much smaller investor thinking about whether you should invest in fund X, and you see that the EIF has given it the full treatment and passed it, you are relatively relaxed and you think, 'I don't need to do the same'."[42]

40. Giles Derrington, Head of Policy at techUK, agreed, and explained that the EIF's willingness to enter the market at an early stage meant that it had "a crowding-in way of working". This was one of the key ways in which the EIF could generate additional investment from the private sector: "It

36 Written evidence from The Infrastructure Forum (EIB0007)
37 Q 25
38 Written evidence from the Welsh Government (EIB0004)
39 Q 7
40 Q 77
41 Q 46
42 Q 44

says, 'We are putting this amount of money into this fund. You can take our commitment to others and say, 'Look, they are going in; it is a green light for you to invest'' … The importance of the EIF in general, and in how it supports [venture capital], is that it is not just about the money, but the signal it sends about the market."[43]

41. **The independent expertise and high-quality due diligence of the EIB and EIF are essential for crowding in private investment. Their participation in specific projects provides a stamp of approval and a positive signal to the market, thereby encouraging additional investment from the private sector. If these institutions stop supporting projects in the UK after Brexit, the Government must ensure that means to replicate their independent expertise and due diligence continue to be available.**

43 *Ibid.*

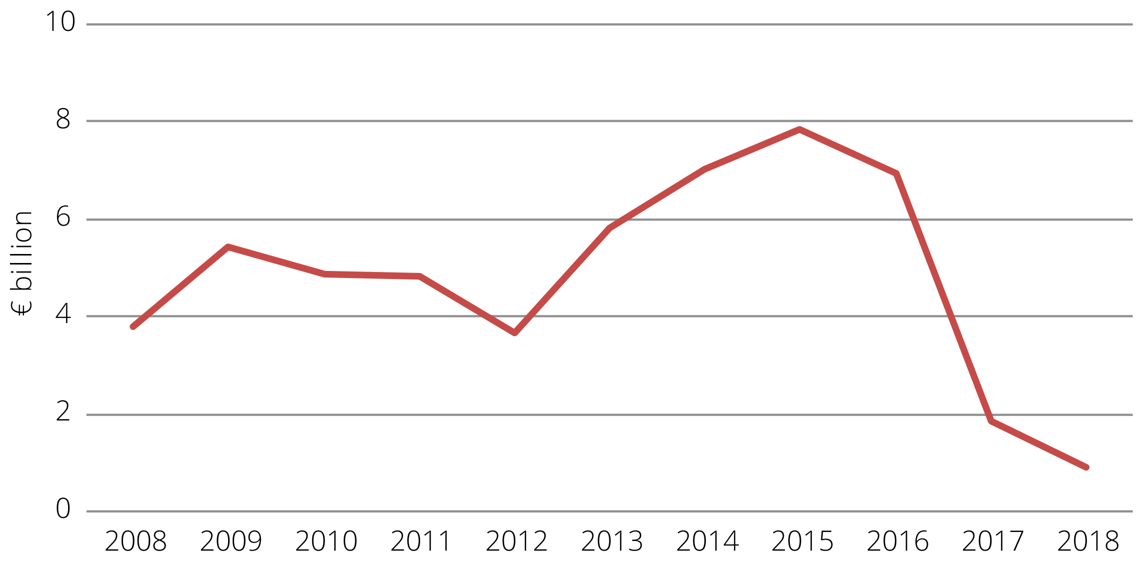
CHAPTER 3: THE IMPACT OF BREXIT ON THE UK'S RELATIONSHIP WITH THE EIB

42. Brexit has already had a material effect on the UK's relationship with the EIB. This chapter considers those effects before turning to review the provisions in the Withdrawal Agreement concerning the EIB's repayment of the UK's capital. Finally, we survey options for the UK's post-Brexit relationship with the EIB.

Lending since the referendum

43. Many witnesses told us of a substantial reduction in EIB and EIF funding since the EU referendum and the triggering of Article 50. In 2015, the EIB lent €7.8 billion to 47 projects in the UK; in 2016 it lent €7 billion to 54 projects. This contrasts with €1.8 billion lent in 2017 to 12 projects and €932 million in 2018 to 10 projects. This represents a decline in EIB lending of approximately 88 percent in three years.[44]

Figure 2: EIB lending to the UK, 2008–2018



Source: European Investment Bank

44. There has been a corresponding reduction in EIF funding. The BVCA stated: "Pitchbook data from February 2018 shows that the total capital raised by Europe's venture groups fell by a quarter in 2017 to €7.4 billion and the total number of new funds dropped to a 10-year low of 54 in 2017, compared with 75 in 2016."[45] Tim Hames, the BVCA's Director General, told us: "There is no question but that the referendum, never mind the actual date of Brexit, has already had a pretty fundamental impact. EIF investment in the UK fell by 91% between 2016 and 2017, which is a large enough number to make you suspect that it was not an accident or a coincidence of timing."[46]

45. The reduction in the EIB's lending may reflect uncertainty as to how contracts will be governed after the UK's departure. As Energy UK said, the

44 European Investment Bank, 'Financed projects: multi-criteria list': http://www.eib.org/en/projects/loan/list/index.htm [accessed 18 December 2018]
45 Written evidence from the British Private Equity and Venture Capital Association (EIB0009)
46 Q 43

reduction "is likely due to the EIB adding guarantees to loans as a result of the UK's withdrawal".[47] This was also the view of the Welsh Government: "The [EIB] is clearly concerned about its immunities and privileges to such an extent that a great many approved UK deals are not being signed."[48]

46. Currently, EIB loan contracts are automatically governed by Union law by virtue of the UK's EU membership. But David Lunn, Director for EU Exit at HM Treasury, confirmed that after the UK's decision to withdraw "the EIB changed the approach it took to UK loans, and new clauses were introduced in contracts with UK borrowers protecting their privileges and immunities after exit", which "had an impact on the willingness of UK [borrowers] to take out these loans, and on the general relationship with the EIB."[49] Piers Williamson cited the Wheatley Group, a Glasgow housing association, which had "closed a deal", but with "some very unusual pre-payment events linked to the nature of Brexit". This meant that, even when a loan was on offer, "Borrowers are quite reticent to draw these loans ahead of certainty on Brexit."[50] Negotiations are also taking longer, and Philip Harding gave the example of UCL, which began negotiating a loan with the EIB in 2015, when it was known that there would be a referendum:

> "We spent quite a bit of time with the European Investment Bank on pre-payment terms and the events that would cause a prepayment. We ensured that the outcome from our point of view was one whereby, if we left the EU, which was still uncertain at that stage, under any circumstances, the terms of our loan would be completely unaffected. We were very careful to make sure that the drafting of our loan was fully Brexit proof."[51]

47. An increase in due diligence may also have played a role in the decline in EIF funding. Victoria Roberts, from Innovate Finance, noted the "press reports in which the EIF said that additional due diligence is now being undertaken on UK funds".[52] In contrast, Mr Hames doubted that the decline in funding could be entirely attributed to an increase in due diligence:

> "It is certainly true, as Victoria said, that the EIF line is that it is only additional due diligence, but when there is a 91% fall between year A and year B, one suspects that the additional due diligence is to check every week, 'Are they still British?' A 91% fall is a moratorium that dare not speak its name. You do not make it 100% because that would be too obvious."[53]

48. Some witnesses seemed unclear on whether existing EIB loans would be affected by the UK's exit; others questioned whether loans that had been approved in principle could be drawn on before the end of any proposed transition period. For example, Universities UK asked that "the UK government press for assurances that UK universities with existing loans will not be impacted by the UK's exit from the EU and that they will not break existing covenants by seeking out alternative funding sources".[54] The East

47 Written evidence from Energy UK (EIB0011)
48 Written evidence from the Welsh Government (EIB004)
49 Q 87
50 Q 21
51 Q 22
52 Q 47
53 *Ibid.*
54 Written evidence from Universities UK (EIB0008)

of England European Partnership stated: "In the short to medium-term, a key worry of current EIB debt holders in the East of England is knowing with cast-iron certainty what will happen to existing finance contracts with the EIB in the short to medium term, irrespective of what type of Brexit is implemented from March 2019."[55] In contrast, some witnesses had received assurances: UCL's Philip Harding said universities had been told by the EIB that "no matter what the terms of Brexit are, the terms of their loans will be unaffected".[56]

49. On the effect of Brexit on existing loans, Article 118 of the Withdrawal Agreement specifies that the existing "privileges and immunities" that apply to the EIB shall continue to apply to loans made before the end of any transition period.[57] And on loans that had been approved but are unsigned, Article 151 states that:

> "The signature of financial operations relating to the United Kingdom, to United Kingdom entities, or to United Kingdom projects approved by the EIB group before the date of entry into force of this Agreement, may take place after that date on the same basis as that on which they were originally approved."[58]

50. The Minister confirmed the effect of these provisions. He told us that "projects that have already been financed will continue to be supported", whereas those which have been approved before exit date "will be able to be signed and financed during the implementation period."[59] Guidance from the Government published on 10 January 2019 also noted that, in the event of a 'no deal' Brexit, the EIB's operating rights for UK projects are preserved through section 4 of the EU Withdrawal Act 2018, meaning that "existing UK project contracts should be protected and organisations do not need to take any action."[60]

51. **There was a marked decline in funding from the EIB and EIF after the referendum and triggering of Article 50, which appears to go beyond what could be explained by the increased due diligence for UK projects. The scale of this decline suggests that there may be financing gap in the UK for projects that have previously benefited from investment by the EIB and EIF.**

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55 Written evidence from the East of England European Partnership (EIB0006)

56 Q 22

57 These privileges and immunities are those in Article 21 of Protocol (No 7) on the Privileges and Immunities of the European Union, Treaty on the Functioning of the European Union, which provides that: "The European Investment Bank shall in addition be exempt from any form of taxation or imposition of a like nature on the occasion of any increase in its capital and from the various formalities which may be connected therewith in the State where the Bank has its seat. Similarly, its dissolution or liquidation shall not give rise to any imposition. Finally, the activities of the Bank and of its organs carried on in accordance with its Statute shall not be subject to any turnover tax."

58 Agreement on the withdrawal of the United Kingdom of Great Britain and Northern Ireland from the European Union and the European Atomic Energy Community as endorsed by leaders at a special meeting of the European Council on 25 November 2018 (25 November 2018): https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/759019/25_November_Agreement_on_the_withdrawal_of_the_United_Kingdom_of_Great_Britain_and_Northern_Ireland_from_the_European_Union_and_the_European_Atomic_Energy_Community.pdf [accessed 4 January 2019]

59 Q 77

60 HM Government, 'Guidance: European Investment Bank Group financing if there's no Brexit deal', 10 January 2019: https://www.gov.uk/government/publications/european-investment-bank-group-financing-if-theres-no-brexit-deal [accessed 22 January 2019]

52. **For ongoing projects, we recognise that the Withdrawal Agreement safeguards existing loans as well as those approved but not made prior to Brexit. If the Agreement is not approved, the Government notes that existing UK projects should be protected through section 4 of the EU Withdrawal Act 2018 and that affected organisations do not need to take any action in this regard. We are however disappointed that this announcement was made on 10 January, with only 78 days until Brexit, and gave no indication about possible replacements for EIB funding.**

The return of the UK's capital

53. As the EIB's shareholders, Member States have committed to €243.3 billion in capital. Of this, €21.7 billion is paid in, the rest callable by the Board of Directors in the event of this being necessary for the EIB to meet its obligations. The Withdrawal Agreement provides that the UK will receive its share of the EIB's paid-in capital in 12 annual instalments (11 of €300 million and a final instalment of approximately €196 million), from December 2019 until 2030. This comes to a total of just under €3.5 billion, representing the UK's 16.1 percent share of the EIB's paid-in subscribed capital, without interest or dividends. The UK will remain liable throughout the period for the uncalled subscribed capital. The amount for which the UK will be liable will depend on the underlying events that trigger the liability, specifically whether they are attributable to financial operations approved by the EIB before the entry into force of the Withdrawal Agreement (calculations are also included for liabilities that will not reduce over time).

54. The EIB has been profitable over its life, raising the question of whether the UK might be expected to benefit from a share of these profits. We asked the Minister whether the Government had attempted to secure any share of the retained earnings of the EIB, which at the end of 2017 stood at approximately €47.3 billion. A 16.1 percent share of those retained earnings would have amounted to approximately €7.6 billion, more than twice the paid-in capital.

55. David Lunn, Director of EU Exit, HM Treasury, told us that the UK's capital could not be compared to an investment in a private sector entity, emphasising that "there is nothing in the treaty and the EIB statutes that says what happens when the shareholder leaves the bank, and how the shareholder gets his money back".[61] He was then pressed further on this point:

> "Clearly, we are aware of how you would value a shareholding in a conventional organisation. All I can say is that this is not a conventional organisation, and the negotiation was driven by the statute and our rights under that statute. I am not sure that there is much more I can say".[62]

56. **Under the Withdrawal Agreement, the UK will receive the capital it has paid in to the EIB but not any share of the profit, as reflected in the retained earnings, nor any interest or dividends for the 12-year period over which the capital will be repaid. While we recognise that this was part of a complex and wide-ranging negotiation on the financial settlement, and that the EIB's statute is silent on the issue, we regret that the Government failed to provide a cogent explanation of the rationale for the position taken in the negotiations. Given the**

61 Q 78
62 *Ibid.*

substantial amounts of money potentially involved—representing up to 20 percent of the UK's obligations under the financial settlement—we call on the Government to explain in clear terms why it did not press for the EIB's profitability to be taken into account in the final calculation of the financial settlement.

Options for a future relationship with the EIB

57. Article 151 of the Withdrawal Agreement effectively precludes EIB financing in the UK post-Brexit, stating that "entities established in the United Kingdom shall be treated as entities located outside the Union".[63]

58. Several witnesses considered options for a future relationship with the EIB. The most ambitious would involve amending the EIB's statute to allow the UK to be a member of the EIB despite not being a Member State. This, however, runs contrary to Article 308 TFEU, which states that "the members of the European Investment Bank shall be the Member States".[64] So while Energy UK believed that "the option of attempting to secure a change to the EIB's statute to allow UK membership will be part of the wider negotiations on the future EU-UK relationship",[65] this seems a remote prospect as it would require EU Treaty change.

59. An alternative would be a third country agreement. Under such an agreement, the EIB would be able to lend to UK borrowers, despite the UK no longer being a Member State. For example, the EIB funds projects in the European Free Trade Association (EFTA) countries through the EFTA Loan Facility, providing €4.2 billion of lending since its creation in 1994. The EIB also provides lending to developing countries, and the Infrastructure Forum noted that "the Cotonou Agreement between the European Commission and the 79 African, Caribbean and Pacific countries provides a model which the UK could replicate".[66] However, it was accepted that the EIB's lending to third countries was far lower than to Member States. As E3G, the energy consultancy, told us: "Although the EIB does lend to non-EU and non-EFTA countries, this makes up only approximately 10% of total lending"—in 2016 this totalled €8 billion.[67]

60. Another option, considered by E3G, was that of establishing a UK EIB subsidiary. The EIB has been reported as considering the establishment of a subsidiary, to focus on non-EU development projects generally, and to lend approximately €7–8 billion a year.[68] However, Mr Clutton-Brock acknowledged that a focus on development would make it "quite hard for the UK to make a strong pitch that it would be a natural home for receiving such finance".[69] For the Government, Mr Lunn told us:

> "It is a thought we are aware of, but it is not something we have done huge amounts of active work on to date. It would be part of the conversation with the EIB, but, as I say, it would depend in part on what the wider

63 Withdrawal Agreement, 25 November 2018, Article 151
64 Article 308, Treaty on the Functioning of the European Union
65 Written evidence from Energy UK (EIB0011)
66 Written evidence from The Infrastructure Forum (EIB0007)
67 Written evidence from E3G (EIB0013)
68 Marc Jones and Francesco Guarascio, 'European Investment Bank plans internationally-focussed offshoot', *Reuters* (6 December 2017): https://uk.reuters.com/article/uk-eu-eib-exclusive/exclusive-european-investment-bank-plans-internationally-focussed-offshoot-idUKKBN1E02XE [accessed 19 December 2018]
69 Q 23

> relationship looks like. In a world where there was a closer relationship, there could be more imaginative solutions such as that, but we have not progressed far on it as yet."[70]

61. There have also been suggestions that the UK should push to create a new multilateral development bank, which could cooperate with the EIB on cross-border European projects.[71] E3G told us that the UK could seek to attract geographically close, non-EU states—such as Iceland, Norway and Switzerland—as potential shareholders, as well as EU Member States that receive proportionally less funding from the EIB than others. In the energy sector, such a bank could support collaboration on projects like the North Sea Offshore Grid and the proposed Iceland-UK interconnector, as well as provide financing to new low-carbon infrastructure within the shareholder countries. Energy UK agreed that a new infrastructure bank supported by the UK, EEA countries and willing EU countries "could become a strong partner to the EIB in transforming Europe's infrastructure and economy".[72]

62. The EIF's mandate requires that 80 percent of funding must be spent within the EU, leaving 20 percent (approximately £460 million) which could potentially be accessed by the UK post Brexit. However, techUK's Giles Derrington told us that the UK would be "competing with the US, Japan and elsewhere",[73] while the BVCA noted that it is "unlikely that the EIF will be able to continue to invest in funds that have a primary investment focus in the UK even if some form of future relationship is maintained".[74] The BVCA's Tim Hames concluded:

> "To be blunt, can I conceive of a world in which the UK, in those sorts of circumstances, would be a 35% recipient of the overall fund? No; it just will not happen. Is it worth going through convoluted arrangements in which we are going to end up putting in more money than we will probably get out? Probably not."[75]

63. The President of the EIB, Werner Hoyer, has been reported as saying that "he would be 'extremely sad' if the idea of continued UK participation in the [EIB] was dead in future", adding that "the portfolio in the UK is excellent".[76] Yet the Government has to date proposed nothing of substance on its preferred relationship: the Government's Chequers plan contained nothing on the EIB and the Political Declaration on the framework for future UK-EU relations, published on 22 November 2018, says only that "the Parties note the United Kingdom's intention to explore options for a future relationship with the European Investment Bank (EIB) Group".[77]

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70 Q 79
71 Written evidence from E3G (EIB0013)
72 Written evidence from Energy UK (EIB0011)
73 Q 45
74 Written evidence from the British Private Equity and Venture Capital Association (EIB0009)
75 Q 48
76 Chris Giles and Jim Pickard, 'European Investment Bank wants UK to remain a member', *Financial Times* (11 July 2018): https://www.ft.com/content/24a5c5c0-8441–11e8-96dd-fa565ec55929 [accessed 5 December 2018]
77 HM Government, Political Declaration setting out the framework for the future relationship between the European Union and the United Kingdom (22 November 2018): https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/758556/22_November_Draft_Political_Declaration_setting_out_the_framework_for_the_future_relationship_between_the_EU_and_the_UK__agreed_at_negotiators__level_and_agreed_in_principle_at_political_level__subject_to_endorsement_by_Leaders.pdf [accessed 19 December 2018]

64. **Article 308 TFEU clearly states that only EU Member States can be members of the EIB. Continued UK membership of the EIB would therefore require a change to the EU Treaties, making it highly unlikely. Our figures show that the EIB's activity in the UK has already fallen by 87 percent since 2016, and by 91 percent for the EIF. At this late stage in the process of the UK's withdrawal from the EU, we are concerned that the Government has said so little about the UK's future relationship with the EIB and disappointed by its lack of ambition in this regard.**

65. **The starting point of any future relationship is that the UK will be a third country. While existing EIB agreements with third countries—notably the states of the European Free Trade Association (EFTA)—provide precedents, the Government should also urgently explore options for a deeper bilateral relationship. Concluding a third country agreement should be an immediate priority, to enable some EIB lending to continue, albeit at a reduced level, as a temporary measure.**

CHAPTER 4: THE CONSEQUENCES OF LOSING ACCESS TO THE EIB

The possible replacement by the private sector

66. As set out in Chapter 2, the EIB has played a significant role in the UK economy in the last 20 years and particularly over the last decade. This raises the prospect that there could be a financing gap both for infrastructure projects and SMEs once the UK loses access to the EIB after March 2019; indeed, the decline in funding since 2016 suggests that this gap may already be materialising.

67. Robert Jenrick MP, Exchequer Secretary to the Treasury, believed that some of the EIB's activities could be replaced after Brexit by either the private sector or by existing Government schemes. He said that the UK currently had "flourishing capital markets for infrastructure, where government-backed or government-endorsed infrastructure projects in particular, or those of public utilities, do not struggle to raise finance". But Mr Jenrick also acknowledged that the EIB was "an important contributor to financing our infrastructure",[78] adding that the Government "do not underestimate the fact that there will be, or might be, a gap in the market that we would want to move into".[79]

68. The Infrastructure Forum agreed that the private sector could play a greater role, noting that routine project finance outside of economic downturns is available from the private banking sector for "most current users of EIB loans", albeit at "significantly higher cost". It cited utilities markets as one example where it would be "relatively straightforward to replace EIB finance". However, it estimated that this would increase the cost by 0.5–1.0 percentage point above the rate of interest offered on EIB loans, a cost which would ultimately be passed on to consumers.[80]

69. James Richardson, Chief Economist at the National Infrastructure Commission, explained that some sectors borrowed substantial amounts from the EIB simply because it was cheaper. In the water and sewerage sector, for example, he noted that funding for Thames Water could be provided "perfectly well by the private finance markets", though this might come at a cost:

> "I find it hard to believe that those projects could not be financed elsewhere. It is a regulated asset base and a pretty stable income stream. These are bankable projects, but they may have to pay a slightly higher rate for that, and that will inevitably feed through to consumers depending on the way the regulator treats the cost of capital. Those would be the impacts."[81]

70. Witnesses from the water industry confirmed that losing access to the EIB was not a major concern. In August 2017 Anglian Water Services became the first European utility company to issue a green bond, allowing it to meet its financing needs competitively. Despite the sharp decline in EIB funding

78 Q 79
79 Q 77
80 Written evidence from The Infrastructure Forum (EIB0007)
81 Q 7

since 2017, their ability to secure affordable finance and to raise finance from international sources has not been diminished.[82]

71. This may not be true for other sectors. Mr Richardson told us that, while in many cases organisations may be able to secure alternative sources of finance, "we are concerned about … those areas where particularly you are bringing forward new technologies, and where actually it may be rather harder to find private finance".[83] Peter Clutton-Brock, of E3G, told us that the ability of the EIB to take on some of the project and technology risk is "a major contributing factor" for attracting private investors.[84]

72. Some sectors within the EIB's broader social mandate may also struggle to raise finance in the private sector. The Infrastructure Forum noted that its members responsible for social, environmental and housing projects would find it "much more difficult" to replace EIB funding.[85] Piers Williamson, Chief Executive of The Housing Finance Corporation, which has worked extensively with the EIB, said that certain phases of regeneration "might not happen" without the EIB's cheaper financing.[86]

73. Concerns were also raised by the higher education sector. Philip Harding, Director of Finance and Business Affairs at UCL, had "no doubt" that there would be a diminution in the rate of investment by universities if access to the EIB were lost.[87] Universities UK agreed that there would be a "noticeable lack of similar funding streams" to fund investment in long-term, large-scale projects such as campus redevelopments. They added that existing domestic alternatives "cannot be used to replicate all of this added value" offered by the EIB.[88]

74. The British Private Equity and Venture Capital Association (BVCA) focused on the EIF, but agreed that, if the EIF withdrew from the UK market, "there may be reduced access to funding for venture capital investments in SMEs, especially in companies that require long term financing". High-growth, high-risk industries could be affected, including emerging technology firms, as well as those relying heavily on long-term research and development funding. This could in turn have an impact on the UK's research reputation and talent pool.[89]

75. **The loss of EIB funding after March 2019 will have different effects on different sectors of the economy. Utilities such as water and sewerage may be able readily to access alternative sources of finance, albeit at an increased cost. More innovative projects, or those that fall within the EIB's broader social mandate, may struggle to raise money in the private sector. As part of its ongoing infrastructure finance review, the Government should identify the sectors most exposed to losing EIB access as well as issues related to SMEs' access to finance from the EIF.**

82 Written evidence from Anglian Water Services (EIB0005)
83 Q 2
84 Q 20
85 Written evidence from The Infrastructure Forum (EIB0007)
86 Q 20
87 *Ibid.*
88 Written evidence from Universities UK (EIB0008)
89 Written evidence from the British Private Equity and Venture Capital Association (EIB0009)

Existing UK Government support for infrastructure

76. The main tool currently used by the Government to support domestic infrastructure projects is the UK Guarantees Scheme. Managed by the Government's Infrastructure and Projects Authority (IPA), it can issue up to £40 billion of guarantees to 'nationally significant' projects and is open until at least 2026. The Exchequer Secretary to the Treasury, Robert Jenrick MP, told us the Government had provided up to £1.8 billion in guarantees through this scheme "to a wide range of different projects of similar scope to the EIB's".[90]

77. Mr Jenrick also explained that there was "significant spare capacity" within the UK Guarantees Scheme. While the projects supported need to be 'nationally significant', the Government had applied that rule "generously". Philip Duffy, Director for Growth and Enterprise at HM Treasury, agreed that there were many options to "put back capacity in particular corners of the market that may be struggling".[91] Nonetheless, despite the reduction in funding coming from the EIB, the Scheme had "not had a significant uptake in inquiries" since the referendum.[92]

78. Peter Clutton-Brock from E3G described the UK Guarantees Scheme as "a very useful mechanism", which had "already started to adapt to pick up some of the slack" from the reduction in EIB funding. Its mandate was "quite broadly defined" and could cover projects in areas beyond brick-and-mortar infrastructure, such as skills or buildings for universities. It was now offering construction guarantees, and he was positive that the Scheme could "certainly help to address the vacuum in the short term".[93]

79. UCL's Philip Harding also recognised the Scheme's importance, describing it as a "valuable source of additional support for higher education".[94] However, he noted the potentially high threshold of 'nationally significant' projects; this has led some stakeholders, such as Energy UK, to call on the Government to "review the remit of the scheme and the eligibility criteria to compensate for the loss of access to similar services in the EU."[95]

80. The Infrastructure Forum also argued that the Government should extend the UK Guarantees Scheme, empowering it to provide more extensive guarantees during the construction phase of projects, as well as to begin to utilise its powers under the Infrastructure (Financial Assistance) Act 2012 to provide loans to infrastructure projects. This, it said, "could replace EIB lending which is no longer available".[96]

81. The Government could also consider changes to the Public Works Loans Board (PWLB), which provides loans to UK public bodies within a policy framework set by HM Treasury. Alex Conway, Assistant Director of Brexit and European Programmes, at the Greater London Authority, urged the Government to "augment" the PWLB by enabling it to offer loans at a discount on its standard concessionary rate.[97] The Infrastructure Forum

90 Q 77
91 Q 79
92 Q 80
93 Q 25
94 Q 24
95 Written evidence from Energy UK (EIB0011)
96 Written evidence from The Infrastructure Forum (EIB0007)
97 Q 24

similarly called for "extending the mandate" of the PWLB to allow it to issue loans to domestic infrastructure projects.[98]

82. **In the short term, the Government should take urgent measures to minimise any financing gap for UK infrastructure. This could include extending the UK Guarantees Scheme to projects that may not meet the current threshold of being 'nationally significant' and allowing it to offer different financing options, given its low take up. The Government should consult with affected industries on how the UK Guarantees Scheme could be improved, with a view to incorporating changes to the Scheme in its forthcoming National Infrastructure Strategy.**

The British Business Bank and SME financing

83. The British Business Bank (BBB) was established in 2014 with the objective of supporting access to finance for SMEs. It operates under its own trading name through a number of subsidiaries. The BBB, in its 2018 Annual Report, identified the possibility of losing access to the EIF as a "strategic risk". Not only does the EIF participate in many of the markets that the BBB operates in as a co-investor, but it also acts as a guarantor for some of the BBB's own programmes. The BBB therefore stated that "if the EIF withdraws from the UK market this may have an impact on the delivery and the risk profile of the Bank's programmes individually or the Bank's portfolio in aggregate".[99]

84. The BVCA set out the view of several witnesses:

> "The EIF has been an active investor in UK venture capital and private equity funds for a long period, and we believe that the British Business Bank (BBB) should look to replicate the EIF's investment programme where possible, and be given the funding to fill the gap created by the withdrawal of the EIF's investment into UK funds."[100]

85. In the 2017 Autumn Budget, following the Government's Patient Capital Review, the Chancellor committed £2.5 billion for patient capital to the BBB.[101] In the 2018 Autumn Budget he announced further new funding, including an extension of BBB funding for the Start Up Loans programme until 2021, and a commitment to make available up to £1 billion of guarantee support via specialist and high street lenders to smaller housebuilders, to be deployed through a variant of the BBB's ENABLE Guarantee programme.[102] The Chancellor also committed up to £200 million of additional investment in venture capital and growth finance in 2019/20 if there is no agreement with the EIF when the UK leaves the EU on 29 March 2019.

86. Keith Morgan, Chief Executive of the BBB, noted that there had been a threefold increase in the BBB's lending capacity since the referendum, from

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98 Written evidence from The Infrastructure Forum (EIB0007)

99 British Business Bank, *Annual Report and Accounts 2018: delivering more for smaller businesses across the UK* (19 July 2018): https://annualreport2018.british-business-bank.co.uk/uploads/documents/BBB_Annual_Report_2018.pdf [accessed 10 December 2018]

100 Written evidence from the British Private Equity and Venture Capital Association (EIB0009)

101 Q 56: Catherine Lewis La Torre, Chief Executive of BBB Patient Capital Holdings, told us that patient capital refers to "long-term, primarily equity, investment [where] you have to be patient to have a return on your capital."

102 The ENABLE Guarantees programme is designed to encourage lending to smaller businesses through a Government-backed portfolio guarantee to cover a portion of banks' net credit losses in excess of an agreed 'first loss' threshold.

£300 million to £930 million. He told us that, in comparison, the BBB's "estimation of [the EIF's] activities on average over the last five years in similar areas is £460 million in this country."[103]

87. As noted above (see paragraphs 38–39), the benefits of the EIF are not just a matter of the money invested; there is also the crowding in effect, deriving both from the robustness of its due diligence and from its involvement early in the financing process. Tim Hames, Director General of the BVCA, told us that "because [the BBB] is three years old and not 24 years old" it does not replicate these benefits.[104] And as techUK's Giles Derrington told us: "the British Business Bank has a tendency to work as an investor of last resort, saying, 'You go away and get the rest of the money, and then come to us if you have a gap and we will fill it', which means you need to try to fill it 100% effectively."[105]

88. Catherine Lewis La Torre, Chief Executive of BBB Patient Capital Holdings, believed that such criticism "probably reflects how we were operating two years ago … it does not reflect what we do today". She explained that the BBB was increasingly playing the role of a cornerstone investor, engaging early with the general partner and fund manager, "and making sure that we do detailed due diligence that other investors may rely on to come in alongside us". At the same time, she acknowledged that this "may not be widely known in external markets".[106] David Lunn, Director of EU Exit, HM Treasury, made similar points.[107]

89. Although witnesses broadly welcomed additional financial commitments from the Government and the move towards earlier involvement in the investment process, Mr Hames noted that these benefits would not be immediately realised:

> "First, there is a challenge for the BBB in scaling itself up fast enough to deal with the challenge. The BBB has been around for only three years. The Chancellor makes an announcement, such as the one in the last Budget, that there is a patient capital fund of £2.5 billion to be deployed over a decade. Understandably, if you are a fund manager, you say, 'That's good news. Where's the queue?' Then you see that there is not yet a structure, or that there is now a structure but not a leadership team; or that there is a structure and a leadership team, but they are not quite sure they have nailed down the mandate and the mission precisely."[108]

Moreover, some recipients of EIF funding may not have experience of interacting with the BBB: "The challenge for the BBB is to make the process of navigation less complicated rather than more complicated."[109]

90. Finally, the BBB also manages regional development funds—the Northern Powerhouse Investment Fund (£400 million), the Midlands Engine Investment Fund (£250 million) and the Cornwall and Isles of Scilly Investment Fund (£40 million)—supported in part by a loan from the EIB

103 Q 55
104 Q 44
105 *Ibid.*
106 Q 62
107 Q 84
108 Q 44
109 Q 51

and a grant from the European Regional Development Fund. Mr Morgan outlined the steps taken to ensure that these arrangements would remain in place post-Brexit:

> "We were very careful to explore any vulnerability around that at the time the funds were created. We got assurance in the following ways. The first is that the EIB loan is a contract, so that loan will withstand any change in the relationship between the UK and the EU. The second relates to the European Regional Development Fund. HM Treasury explained at the time that it would be prepared to underwrite that funding until 2020 in the event that it was not forthcoming, so in that respect the current structure of these funds is secure."[110]

91. **We welcome the fact that the Government has already announced changes to the resources of the British Business Bank (BBB) as well as its commitment to providing it with additional funding when the UK loses access to the EIF. The BBB told us that it is increasingly acting as a cornerstone investor that crowds in private investment, but this view did not appear to be shared by some industry stakeholders. Greater efforts to demonstrate that it is available to fulfil the functions of enhanced due diligence and acting as a cornerstone investor may be required and the BBB should make clear how it measures success in this regard.**

110 Q 57

CHAPTER 5: ESTABLISHING A UK INFRASTRUCTURE BANK

Renewed calls for an independent UK infrastructure institution

92. In a recent report, The Infrastructure Forum's EIB Working Group argued that the creation of a 'British Investment Bank' could in the long term deliver the 'soft' benefits currently provided by the EIB, notably its role as a cornerstone investor, fostering confidence for investors and facilitating projects that may not otherwise achieve sufficient funding.[111]

93. Several witnesses to our inquiry indicated their support for creating a new infrastructure institution (see Box 2 for examples of such institutions in other countries). The East of England European Partnership, for example, called on the Government to support "the greatest plurality of finance and funding options … possible" for local authorities, but also noted that a single domestic replacement for the EIB and EIF "would be broadly welcomed".[112] It is notable that the Scottish Government has already decided to a create a Scottish National Investment Bank in order to raise infrastructure investment.[113]

94. From the education sector, Universities UK noted that there were "many benefits to establishing a national-level investment bank", in the event that the UK loses access to the EIB.[114] Unite called for the creation of a state investment bank to fund an expansion of UK housebuilding.[115] Energy UK noted that the Government could consider contributing towards the creation of a new multilateral infrastructure bank alongside the EIB,[116] something also explored by researchers at E3G.[117]

95. Significantly, the idea of a creating a new infrastructure bank has also received backing from the National Infrastructure Commission (NIC). In July 2018 the NIC published its first *National Infrastructure Assessment*, setting out key objectives and priorities for the UK over the next 10–30 years. Referring to the funding and financing of projects, it noted that there existed "an ongoing market failure around innovation in the infrastructure sector; the risks associated with innovative technologies, techniques and financial products can be too high for the private sector without government support".[118]

111 The Infrastructure Forum, *The Future of the European Investment Bank in the UK: report by The Infrastructure Forum's EIB Working Group* (2017): https://docs.wixstatic.com/ugd/d9a995_9e8ae46e9a6f44f89e1b0d23d0c271ee.pdf [accessed 4 January 2019]
112 Written evidence from the East of England European Partnership (EIB0006)
113 Written evidence from the Scottish Government (EIB0010)
114 Written evidence from Universities UK (EIB0008)
115 Written evidence from Unite the Union (EIB0012)
116 Written evidence from Energy UK (EIB0011)
117 Written evidence from E3G (EIB0013)
118 National Infrastructure Commission, *National Infrastructure Assessment* (10 July 2018): https://www.nic.org.uk/wp-content/uploads/CCS001_CCS0618917350–001_NIC-NIA_Accessible.pdf [accessed 4 January 2019]

Box 2: National promotional banks in other developed economies

Many other countries have their own national promotional banks to encourage investment in their domestic economies. In addition to Germany's KfW (see Box 4), the below lists some comparable institutions in other jurisdictions.

Nordic Investment Bank (Denmark, Estonia, Finland, Iceland, Latvia, Lithuania, Norway and Sweden): The NIB's vision is to create "a prosperous and sustainable Nordic-Baltic region", and its mission is "to finance projects that improve competitiveness and the environment of the Nordic and Baltic countries". Established in 1976, it is 100 percent owned by the eight Nordic and Baltic states in the NIB, with share-holdings depending on the size of the state. In 2017 it held assets of €29.9 billion. Annual lending in 2017 was €3.7 billion.

Cassa Depositi e Prestiti (Italy): In February 2017, the CDP announced a new mission to "promote Italy's future by contributing to economic development and investing in competitiveness." Established in 1850, it is 83 percent owned by the state (Ministry of the Interior), 16 percent institutional investors and 1 percent in Treasury shares. In 2018 it held assets of €366 billion. Annual lending by the CDP in 2018 was €13 billion.

Bpifrance (France): Bpifrance has three goals, to accompany businesses in their growth, to prepare for future competitiveness and to develop an ecosystem that favours entrepreneurship. It was established in 2012 through the merger of a number of existing public funds and organisations in France. In 2017 it held assets of €52.4 billion in 2017 and it lent €7.2 billion.

There are also a number of examples of such institutions being established outside Europe. The Development Bank of Japan was created in 1999, building on its post-war predecessors, and has a strong focus on infrastructure. More recently, the Canadian Government established a new arm's-length public institution in 2017, the Canada Infrastructure Bank, that will seek to invest $35 billion from the federal government into domestic infrastructure projects.

96. The NIC also said that the Government should try to maintain access to the EIB. If this were not possible, it argued that a new, operationally independent, UK infrastructure finance institution should be established after Brexit. James Richardson, Chief Economist at the NIC, told us:

> "That piece of work was the one that led us to the conclusion that retaining access to the EIB should be the priority, and, if that cannot be achieved, it is time now to start thinking about a plan B, and that there could be a role for a UK investment institution of some kind in filling some of the gap—not necessarily everything but some of the gap—that is currently filled by the EIB."[119]

97. In supplementary written evidence, the NIC clarified that any UK infrastructure finance institution would not have to finance the same proportion of UK infrastructure investment as the EIB. Housing, for example, is not covered by the NIC's remit. Moreover, some EIB lending—especially in transport—goes to UK public sector bodies.[120]

98. The NIC argued that a new institution should be established by 2021, on the basis of a consultation completed by spring 2019. A consultation would cover

119 Q 1
120 Written evidence from the National Infrastructure Commission (EIB0014)

its functions, such as providing finance to economic infrastructure projects in cases of market and coordination failures, as well as ways to catalyse innovation and act as a 'centre of excellence' on infrastructure projects. The NIC says that such an institution would also need to have a clear mandate, with considerations made for its wider economic and social impact, and good governance to safeguard its operational independence.

99. However, Werner Hoyer, the current President of the EIB, has publicly said that, even in a financial centre like London, the creation of any such institution in the UK would take between five and 10 years.[121] The Minister noted that, even after creating the institution, it would take "many years" for it to build up its reputation. This, he argued, could be used as an argument against establishing an infrastructure bank at all:

> "Clearly, it would take some time, and one of the arguments against creating a new stand-alone institution may be that such institutions take time to develop capacity, and to mature and gain the track record of one as long-standing as the EIB. Clearly, it would take a couple of years to establish it and then many years to build up the reputation."[122]

100. The Government has previous experience of establishing a state investment bank in the form of the Green Investment Bank (GIB), set up in 2012 (see Box 3). James Richardson said that a new institution might look "relatively similar to the Green Investment Bank", with a balance sheet that is "certainly in single figure billions". The precedent established by the GIB might make it easier to create a new, similar institution:

> "You are right to say that there is an institutional lifecycle, and to develop all the expertise, culture and so on would take longer than the time it takes simply to establish the body. Equally, you can look at the Green Investment Bank experience and say that this body was set up relatively quickly and did have a material impact on the offshore wind market within a relatively short period of time. You may not get all of the benefits of a well-established body—and of course that is one of the arguments for retaining access to the EIB; you just get to keep that—but, equally, you are certainly getting capability before 10 years."[123]

121 Chris Giles and Jim Pickard, 'European Investment Bank wants UK to remain a member', *Financial Times* (11 July 2018): https://www.ft.com/content/24a5c5c0-8441–11e8-96dd-fa565ec55929 [accessed 5 December 2018]

122 Q 82

123 Q 10

Box 3: The Green Investment Bank

The Green Investment Bank (GIB) was set up by the Government to increase the level of green infrastructure investment in the UK, following the recommendations of the GIB Commission in 2010. The Commission highlighted the "urgent need for a new public financial institution to unlock the investment needed for the UK to deliver a timely transition to a low carbon economy". The GIB was subsequently set up in 2012, with £3 billion of Government funding.

The GIB's 2016–17 Annual Report summarised progress until 31 March 2017, the last accounting year in which it was publicly owned. This included £2.9 billion of investment commitments in 93 UK green infrastructure projects, worth a total of £12 billion. The GIB reported a profit before tax of £24 million and a projected portfolio return of 10 percent per annum.

In June 2015 the UK Government announced its intention to move GIB into the private sector by selling a majority of its shares. In March 2016, the transaction was launched and in April 2017 it was announced that Macquarie Group Limited (Macquarie) would acquire 100 percent of the share capital of GIB. The sale of GIB completed in August 2017 for £2.3 billion, which now has an international rather than a strictly UK focus.

101. In its interim response to the *National Infrastructure Assessment*, published alongside the 2018 Autumn Budget, the Government announced it would review its existing support for infrastructure finance. The Minister told us that the review "will be launched either at the end of this year [2018] or the beginning of next year [2019], and we hope to bring it to a conclusion next year, along with the spending review".[124] The Government will then publish its own National Infrastructure Strategy, which will set out the Government's priorities for economic infrastructure and respond in detail to the NIC's recommendations.[125]

102. **Several witnesses proposed establishing a UK infrastructure bank, if access to the EIB is lost. We note that the National Infrastructure Commission has called for such an institution to be established by 2021. In responding to the NIC's recommendation as part of its infrastructure finance review, the Government should urgently identify and consult on potential market failures in the UK infrastructure market, particularly in areas where the EIB has previously operated. The Government should then explain how it intends to address any market failures, considering in this light the role that could be played by a UK infrastructure bank.**

The benefits of having a UK infrastructure bank

Gaining confidence from private investors

103. The *National Infrastructure Assessment* noted that an independent infrastructure institution could provide policy stability in areas outside the short-term political cycle. The NIC's James Richardson argued that it might be able to take good financial risks in areas that are politically less attractive:

124 Q 82

125 HM Treasury, *Budget 2018: Interim Response to the National Infrastructure Assessment* (29 October 2018): https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/752340/NIA_Interim_Response_pdf.pdf [accessed 4 January 2019]

> "[Independence] is important in terms of the ability of the institution to put a stamp of authority on a project that private investors can then have confidence in that this is an independent institution making financially sound judgments. There is a risk, if all these decisions are being signed off by Ministers, that private investors might think, to put it at its most extreme, 'Is it Concorde?' Is it something that Ministers think is exciting but actually is not a sound investment? You then lose that stamp of approval and the potential benefit that has in terms of bringing other people on board."[126]

104. Academics from UCL's Institute for Innovation and Public Purpose (IIPP), which has produced comparative research on how state investment banks operate,[127] argued that independence could ensure the 'long-termism' of such an institution. Josh Ryan-Collins, Head of Research at the IIPP, stated: "To maintain a longer-term focus it is important that it has some independence from the Government of the day, with a governance arrangement whereby people are independent of the Government."[128] Laurie Macfarlane, Public Banking Lead at the IIPP, agreed that independence could allow the institution to focus on its strategic priorities, free from "the day-to-day political mood music of the day that tends to consume the Treasury and other departments … which can often be very distracting".[129]

105. Peter Clutton-Brock, who previously worked on the creation of the GIB as an official in HM Treasury, described distance from Government as "really important", if investors are to be attracted to invest alongside such an infrastructure institution. Independence can "generate the credibility to crowd in other investors", who are often highly concerned about the political risks of decision-making. He noted recent examples, such as the Swansea Bay tidal lagoon project and Hinkley Point C, where Government decision-making processes had been very lengthy.[130]

106. Piers Williamson, Chief Executive of The Housing Finance Corporation (THFC), which has worked extensively with the EIB, also underlined the importance of not being exposed to "political whims" when lending and investing in the longer term:

> "The politics can change a great deal in 30 years, so having an organisation that can act independently of government is important. It does not have to be completely independent of government; there are constructs such as halfway houses and non-departmental government bodies. All those sorts of boxes can be fit for purpose, but some independence is really very important for long-term investment."[131]

107. UCL's Philip Harding, on the other hand, noted that there was "some value" to proximity to Government,[132] while Giles Derrington, Head of Policy at techUK, highlighted the value of a good relationship with Government, on

126 Q 3
127 Laurie Macfarlane and Mariana Mazzucato, *State investment banks and patient finance: An international comparison* (2018): https://www.ucl.ac.uk/bartlett/public-purpose/sites/public-purpose/files/iipp_wp_2018-01.pdf [accessed on 17 January 2019]
128 Q 32
129 Q 38
130 Q 25
131 *Ibid.*
132 *Ibid.*

issues such as its Industrial Strategy.[133] Laurie Macfarlane, from the IIPP, told us:

> "It is about striking the right balance of political representation. On the one hand, you want some sense of democratic accountability while being able to align with government priorities, but, on the other hand, you want to make absolutely sure that it is not run or swayed by day-to-day political interests, and that it is free to make independent banking decisions based on sound financial principles. That is a really important part, and it should be considered very carefully."[134]

108. When we put these points to the Exchequer Secretary to the Treasury, he noted that there could also be a "stamp of approval" for projects coming through the Infrastructure and Projects Authority (IPA) and HM Treasury.[135] Philip Duffy, Director for Growth and Enterprise at HM Treasury, agreed that "just as with the EIB, there is beginning to be a halo effect" around the IPA's due diligence. He added that the UK Guarantees Scheme "currently provides a high level of independence in credit scoring for guarantee schemes, before they come to the Treasury, so there is already a bit of independence. It is not the case that it is working wholly under the Treasury's instructions."[136]

109. **There could be significant benefits to having an infrastructure institution that is independent from Government, particularly with respect to individual investment decisions, thereby generating greater confidence from investors, particularly for long-term projects, and crowding in investment from the private sector. Such an institution would need to be free from day-to-day political interests, though should be aligned with clearly defined strategic national priorities.**

110. **As part of its infrastructure finance review, the Government should clearly identify the areas where an independent infrastructure institution could deliver benefits, particularly given any loss of access to the EIB. Depending on the results of its review, we urge the Government to consult on the establishment of an independent UK infrastructure bank as part of its National Infrastructure Strategy.**

Attracting expertise

111. We have discussed the importance of the EIB's expertise and due diligence, particularly in crowding in additional investment from the private sector. Attracting comparable expertise would be key for any UK infrastructure bank. Phil Graham, Chief Executive of the NIC, told us that, alongside independence, this need for expertise "led us to the conclusion that there is a case for a targeted investment institution".[137] James Richardson explained this further:

> "The other thing that you get with an independent institution is it is probably easier to attract expertise. Inevitably, it is hard to pay civil servants in the Treasury or wherever the kinds of salaries you would for really top people in financial services. It is a little easier, if you create an independent institution, to get around some of those constraints that

133 Q 52
134 Q 36
135 Q 83
136 *Ibid.*
137 Q 15

you probably need to get around if you are hiring people to run a major financial institution with a large balance sheet."[138]

112. Peter Clutton-Brock from E3G explained that the GIB's 'value added', and one of the key arguments that led the Government of the day to establish it, was its ability to provide expertise and analysis to help mainstream investors better understand the technological risks involved in different projects.[139]

113. Laurie Macfarlane also advocated building an institutional hub of expertise "that is independent and distinct, with its own identity, from, for example, government departments". Having an independent institution meant "you can develop specific expertise in the areas where these institutions invest, and employ not just finance people but people who understand and work in the area, whether it is a scientific area, engineering or whatever".[140]

114. The Minister recognised the importance of expertise in crowding in private investment. The Government was already taking measures to address this, and "investing in more expertise in areas such as technology", and there was "significantly more capacity today than there was a few years ago". However, the Minister recognised that expertise remained "an important question that will need to be considered … something we will have to look at in the review".[141]

115. **Witnesses underlined the importance of having sufficient expertise within any national infrastructure institution, enabling it to conduct credible due diligence and be able to give a clear 'stamp of approval' for infrastructure projects. This would give confidence to private investors in the market and thereby crowd in additional investment. Attracting such expertise may be easier for an independent institution than for the Government itself. We urge the Government to take this issue into account as part of its infrastructure finance review and National Infrastructure Strategy.**

Playing a countercyclical role

116. Another area where a UK infrastructure bank independent from Government could add value could be its ability to continue investing in projects through the economic cycle, including during economic downturns, when public budgets may be under pressure. The Infrastructure Forum, for example, told us: "During times of market contraction, the EIB is able to continue to lend when commercial loans dry up. This acts as a stabilising force for markets and keeps financing streams open."[142] Laurie Macfarlane from the IIPP noted that after the financial crisis the EIB stepped up its activities, to offset the downturn in lending across Europe.[143]

117. Eva Witt, Director of Federal and European Affairs at KfW, Germany's state investment bank, cited the KfW's countercyclical role during the financial crisis. Germany used KfW as an "economic stimulus programme", and its success soon generated interest from other governments. In particular, KfW facilitated the provision of long-term finance: "Especially after the financial

138 Q 3
139 Q 25
140 Q 41
141 Q 83
142 Written evidence from The Infrastructure Forum (EIB0007)
143 Q 30

crisis in 2008–09 there was a lack of long tenors. All the banks could access our programmes and give longer tenors to their clients, which at that point they were no longer able to do."[144]

118. James Richardson of the NIC agreed that it helped to have independent institutions in place when unexpected events occur, such as financial crises, because they provided the capacity to act quickly: the UK would have "depth and capability if you had a freestanding institution that would put you in a better position if you were hit by a shock".[145]

119. **One argument for an independent institution is its potential to play a countercyclical role in the event of an economic downturn, during which it could continue to support long-term infrastructure finance and contribute towards the UK's economic recovery. This potential benefit should be recognised as part of the Government's ongoing work in this area.**

Considerations for creating a UK infrastructure bank

Possible barriers

Existing State aid rules

120. The possible creation of a UK infrastructure bank may have to comply with EU State aid rules.[146] While the Commission and the EIB have clarified that financing from the EIB does not constitute State aid, this may not be true for national initiatives.[147] Speaking about the GIB, and whether it could have expanded into other areas of infrastructure, James Richardson from the NIC told us:

> "In retrospect, the ambition was to be broader than offshore wind [but] it needed to fit within State aid and that kind of constraint in what it could do … If it had had a slightly wider remit across all of infrastructure, it might have been able to move on to something like fibre that was outside its green remit but would have met State aid."[148]

121. Although the European Commission approved the GIB under EU State aid rules in 2012, it did so with a number of restrictions. For example, projects applying for funding from the GIB had to prove they had first attempted to obtain funds from the private sector. The Commission also strongly discouraged the inclusion of nuclear energy, as this would have delayed its State aid approval, and stipulated that at least 80 percent of the value of the GIB's investments would have to be deployed through the three 'priority sectors' of offshore wind, waste and non-domestic energy efficiency.[149]

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144 Q 66

145 Q 3

146 The UK would have to fully apply EU State aid rules during the transition period and if the backstop were to be activated. The political declaration on the future relationship between the EU and UK, published on 22 November 2018, also states that the parties "must ensure open and fair competition" with regard to State aid, "building on the level playing field arrangements provided for in the Withdrawal Agreement and commensurate with the overall economic relationship".

147 European Investment Bank, *Joint Statement by Joaquin Almunia, European Union Commissioner for Competition, and Werner Hoyer, President of the European Investment Bank (EIB), on State aid matters in relation to the activities of the EIB Group,* http://ec.europa.eu/competition/state_aid/modernisation/joint_statement_en.pdf [accessed 4 January 2019]

148 Q 6

149 House of Commons Library, *Green Investment Bank: proposed sale*, Briefing Paper Number 5977, 24 January 2017

122. The establishment of the British Business Bank also required State aid approval from the Commission. While this was granted in 2014, the Commission set a £6 billion limit on the amount of funding the BBB could receive from the Government on a non-commercial basis, and set an expiration date of the end of the 2019.[150] Keith Morgan, Chief Executive of the BBB, did not think that this renewal would be an issue and noted the BBB's "responsibility, passed to it by the Government, to ensure that we observe State aid rules".[151]

123. Philip Duffy, Director for Growth and Enterprise at HM Treasury, said that the Government "remain a strong supporter of State aid control", and "do not want public authorities favouring a particular company over another". He added that "some of the desire to be bound by State aid may come from us as much as it comes from our interlocutors in the negotiations".[152]

124. Some witnesses, however, believed that the Government was not sufficiently utilising the flexibility that exists in EU State aid rules.[153] Laurie Macfarlane identified general block exemptions related to the EU's strategic priorities or known market failures, which were roughly the areas where a UK infrastructure bank would operate.[154] He told us that the UK had often "massively underused" the existing allowances:

> "Our State aid expenditure is hardly anything compared with the Scandinavians and Germans. We have taken an overly cautious approach, which again we have imposed on ourselves; we have decided just not to do things, even though we could. There is quite a lot more that we could be doing, even within the current rules. It is an important consideration, but it cannot be used as an excuse for inaction."[155]

125. Germany's national promotional bank, KfW, which has been approved under EU State aid rules, is described in Box 4. Measured by its total assets (€472 billion),[156] it is the country's third largest bank, demonstrating that State aid rules would not prevent the UK from establishing an infrastructure bank. They would, however, have to be borne in mind when designing the institution, and Eva Witt told us that if KfW designed a new programme with the German government, "we would conceive it in such a way that it is State aid free".[157]

126. **If the Government decided to establish a UK infrastructure bank, our future relationship with the EU may require us to respect EU State aid rules when considering its design. This was the case for the Green Investment Bank and continues to set the limits of the British Business Bank's activities. However, the example of some Member States, notably Germany, shows that these rules allow sufficient flexibility to enable the creation of such a national infrastructure institution.**

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150 European Commission State Aid Case SA.36061 UK Business Bank (OJ C 460/3, 19 December 2014)
151 Q 56
152 Q 86
153 See also European Union Committee, *Brexit: competition and State aid* (12th Report, Session 2017–19, HL Paper 67), para 214
154 cf. European Union Committee, *Brexit: competition and State aid* (12th Report, Session 2017–19, HL Paper 67), paras 58–61. This report concluded that "the majority of new State aid measures are now covered by the General Block Exemption Regulation (GBER) and Member States are not required to notify them to the Commission for prior authorisation."
155 Q 40
156 KfW, *Financial Report 2017*: https://www.kfw.de/PDF/Download-Center/Finanzpublikationen/PDF-Dokumente-Berichte-etc/3_Finanzberichte/Finanzbericht_2017-2.pdf [accessed 10 December 2018]
157 Q 69

Measurements of public debt

127. Another possible constraint in creating a UK infrastructure bank would be its impact upon the Government's measure of public sector net debt.[158] James Richardson told us that a new institution would "almost certainly" score in the official public debt estimates, and that "in practice it would be very difficult to take it off public sector net debt as a measure". The definition of public sector net debt used by the Government "makes it pretty hard to escape for an institution of this sort".[159]

128. This contrasts with how national public debt is currently calculated in respect of the EIB. As the EIB's shareholders, EU Member States are legally liable for over €243 billion of liabilities, but these do not score in national balance sheets. James Richardson described it as a "little bit of fiscal magic".[160] Piers Williamson from The Housing Finance Corporation (THFC) went further:

> "One of the benefits of the EIB is that, until recently, it was classified as a remote contingent liability. Effectively, it is off the Government's balance sheet, so it is a fantastic money-printing device for every nation in the European Union. I do not mean that cynically; it genuinely is that. It is about all of those devices if we bring guarantees into the UK public domain."[161]

129. Researchers at E3G argued that this kind of statistical calculation could "jeopardise" the Government's fiscal target of reducing public sector net debt as a proportion of GDP, and reduce funding for other Government departments. They also argued that it was this kind of impact on the Government's balance sheet that resulted in its decision to sell off the Green Investment Bank. This could have serious implications for a new UK infrastructure bank:

> "Whilst it is possible to envisage the government collating existing funding into a single institution, it is hard to imagine such an institution being allowed to substantially increase infrastructure funding because of the effect on the government's fiscal targets. It is also likely that the Treasury would require stringent governance controls and financial restrictions (such as limiting borrowing) to control the impact on the PSND. It may also seek to sell the institution in the future, thereby nullifying its ability to address market failures."[162]

130. In contrast, Laurie Macfarlane argued that the UK's calculation of public debt was "a complete outlier internationally", and something we have "imposed on ourselves", noting that other European countries use the measure of general government gross debt, which does not include the liabilities of public corporations. He also noted that such institutions have assets as well as liabilities. Josh Ryan-Collins explained this point further:

> "A state investment bank could provide equity and require a return on it. A lot of state investment banks clean their backs; they never get into debt

158 Public sector net debt is the official definition used by the Office for National Statistics (ONS) when measuring the Government's outstanding debt obligations. The is often referred to by commentators as 'national debt'.

159 Q 9

160 Q 13

161 Q 24

162 Written evidence from E3G (EIB0013)

> and they are very profitable. The EIB has been extremely profitable. It should not be seen as another cost for the Government; it should be seen as an institution that will create assets, which themselves provide a flow of income to UK plc."[163]

131. James Richardson agreed that a UK infrastructure bank would be expected to make a sufficient return to pay the cost of the interest on the capital paid in, meaning that it would not add to the aggregate debt interest in total. The ONS was currently looking at how assets could be included within the public debt statistics:

> "There is also a measure that this Government have asked the ONS to introduce, public sector net financial liabilities, which would capture both the liabilities but also the assets. You would expect those essentially to balance, so in that sense it would be on the balance sheet but would wash out, and the effect on the balance sheet would therefore be neutralised. If the Government chose to move to that at some point in the future, that would have a different impact. At the moment, it is an experimental ONS statistic, but as it gets traction, it is something the Government may wish to look at."[164]

132. The Minister made it clear that the Government did not intend to remove the liabilities of public corporations from its official measure of public debt. The UK's public sector net debt rules were "well regarded internationally. The IMF and other institutions believe that they are very transparent, and that is a good thing." He also said that this has not previously inhibited public investment, noting that "finding accounting tricks to enable us to invest more in infrastructure but which do not fundamentally change the amount of debt we are taking on as a country is not the way forward".[165]

133. **The EIB's liabilities do not feature on the national balance sheets of EU Member States, but we were told that a similar UK institution would almost certainly feature within the Government's measure of public sector net debt. While such an institution would also have assets and would probably be able to fund the interest on its paid-in capital, this could have significant implications for the Government's commitment to reduce public debt as a proportion of GDP.**

134. **The measure of Government debt does not fall within the scope of this inquiry. While we acknowledge that it is for the Government to choose the best way to calculate public sector debt, such accounting decisions should not determine economic decisions about the optimal form of support for long-term infrastructure investment in the UK.**

Design considerations

Funding options

135. The EIB has the ability to borrow on the capital markets, on the basis of a public sector guarantee provided by the capital subscribed by EU Member

163 Q 34
164 Q 17
165 Q 85

States. This can be contrasted with the BBB and the GIB.[166] As Laurie Macfarlane told us, "Although they are called banks, they are not banks; they are just funds that are allocated money that they are then allowed to lend and spend."[167] He argued that allowing such institutions to issue their own bonds would enable them to leverage their public guarantee and "get more bang for your buck".[168]

136. Eva Witt from KfW, which has been issuing its own bonds since 1949, explained that this 'on-lending model' reduced the borrowing costs for projects: "Being an AAA institution, we fund ourselves on the capital market with a huge volume, so we have cheap funding costs, or cheaper compared with the German banking sector". This cheaper funding was then passed on to commercial banks, subject to certain conditions: "To the degree that it is State aid free and acceptable, we have some sort of subsidy."[169]

137. James Richardson from the NIC, however, noted that any bonds issued an independent institution would be less liquid than UK Government bonds and would probably trade at a premium, making its borrowing more expensive. Indeed, KfW trades at a small premium to the federal Government in Germany. There would therefore have to be a clear reason for allowing such an institution to borrow on the capital markets:

> "There is a cost to it doing that. Is there a commensurate benefit in terms of the kinds of discipline that brings? You would have to be confident that there was for there to be a case for it to issue its own finance. It is not a crazy idea—KfW does it and Transport for London has done it—but there is a cost to it, so you would have to be clear that the benefit was there."[170]

138. Mr Richardson added that any borrowing by an independent institution would feature on the Government's measure of public sector net debt: "Whether it raises its money in the private capital markets or it gets it from the debt management office, as it were, it is all going to score in public sector net debt exactly the same."[171]

139. Keith Morgan, Chief Executive of the BBB, agreed that an independent institution funding itself on the capital markets would cost more than if the Government raised the money through the sale of gilts, and that this borrowing would be consolidated within public sector net debt. Although there could be some "further freedoms" for such an institution, the BBB's

166 In 2014, the GIB's CEO Shaun Kingsbury publicly called for the GIB's borrowing restrictions to be lifted so that it could borrow on the capital markets. Terry Macalister, 'Green Investment Bank boss calls for his borrowing restrictions to be lifted', *The Guardian* (19 June 2014): https://www.theguardian.com/environment/2014/jun/19/green-investment-bank-borrowing-restrictions-60bn-capital-markets [accessed 5 December 2018]

167 Q 34

168 Q 35

169 A 2015 Communication from the European Commission on the role of national promotional banks commented positively on such institutions intervening indirectly via financial intermediaries. This, it noted, reduces the risks of crowding out and discrimination against private finance providers. Communication from the Commission to the European Parliament and the Council, *Working together for jobs and growth: The role of National Promotional Banks (NPBs) in supporting the Investment Plan for Europe* COM(2015) 361 final

170 Q 11

171 *Ibid.*

business plan would require approval from the Government and therefore "the source of funding will not deliver a different BBB".[172]

140. The increased cost of borrowing for an independent institution issuing its own bonds was also noted by Philip Duffy, of HM Treasury: "The gilt market is deep; it is tradable in a way that is not the case for project bonds, and may not be the case for a smaller lender." The Government's answer for many years had been to move utilities into the private sector with a regulator, which "has enabled them to borrow against their infrastructure needs in a regulated way that is off-balance sheet. That remains a very important answer to that particular predicament."[173]

141. **The EIB finances itself on the capital markets, on the basis of a guarantee by EU Member States. This could serve as a possible model for a UK infrastructure bank. While it would almost certainly have higher borrowing costs than the Government itself, there may be compensating benefits. We therefore invite the Government, in considering a UK infrastructure bank, to take into account the advantages and disadvantages of such an institution funding itself on the capital markets.**

A 'one-stop shop'

142. Rather than being solely focused on infrastructure, an independent institution could be merged with other public institutions that are involved in the public provision of finance, such as the BBB and the Public Works Loan Board. It could also cover institutions beyond the scope of this inquiry, such UK Export Finance, which operates as the country's export credit agency.

143. In Germany, for instance, KfW provides an umbrella for a number of subsidiaries split between commercial bank financing, its Mittelstandsbank (SME bank), KfW IPEX-Bank for export finance, and KfW Development Bank and the German Investment Corporation (DEG), which focus on economic development in other countries. In 2017, it created KfW Capital, with the objective of promoting innovation and growth through German and European venture capital and venture debt funds.

144. Eva Witt from KfW identified the benefits of this approach. It created "one point of entry for the client", which made it easier to navigate the different financing options, and also delivered administrative savings:

> "There are joint administration departments. KfW is a regulated bank, so there is a certain cost to that, but being a bigger bank the cost is absorbed more easily than if different institutions were being regulated. You would need a compliance department, an HR department, accountants and so on."[174]

172 Q 61
173 Q 86
174 Q 65

Box 4: An overview of KfW, Germany's state investment bank

KfW is Germany's state investment bank, and is 80 percent owned by the Federal Republic of Germany and 20 percent by the Länder. It was established in 1948 as Kreditanstalt für Wiederaufbau ('Reconstruction Credit Institute'), as part of the Marshall Plan to support post-war reconstruction. Today it focuses on the four areas of climate change and environment, globalisation, innovation and SMEs.

KfW plays an important role in the Germany economy and has provided more than €1 trillion in loans since its creation. Measured by its current total assets of €472 billion, KfW is the country's third largest bank after Deutsche Bank and DZ Bank. It funds its promotional business almost entirely via the international capital markets, and in 2017 raised €78.2 billion for this purpose. Not only has it been granted AAA rating by all major credit rating agencies, but in 2017 *Global Finance Magazine* declared KfW 'The World's Safest Bank' for the ninth year in a row.

145. Laurie Macfarlane from the IIPP told us that—unlike separate entities—a single financing institution could "take advantage of staff and expertise synergies, creating a more coherent landscape for businesses". He saw benefits in having a single entity and a single brand, with specialised departments and arms, and noted that other countries have been moving in this direction:

> "It is interesting to note that, among other countries, moves have been made to consolidate the export credit arm within a wider state investment bank to provide a kind of one-stop shop and get synergies for providing services for businesses. We have seen that happen in France and Italy, bringing things in-house, with the state investment bank thinking more generally about how to help businesses and exports. That is another area where the UK could be doing a lot better, by bringing in UK export finance and wrapping it in a wider approach to public support."[175]

146. Others questioned the synergies that would result from having a single public financing institution. While James Richardson acknowledged the clear benefits of having a single institution for raising money on capital markets, he saw a distinction between facilitating access to finance for SMEs and lending for large infrastructure projects:

> "In a sense, you can always establish institutions in a number of different ways, but the direct overlap between the activities of the British Business Bank and those we would anticipate here is quite limited … The overlap in terms of the kinds of skills and activities is pretty limited."[176]

147. Robert Jenrick MP explained that the Government's existing system of providing financing support focused on "bespoke interventions" in different areas of the economy. However, he noted that there "may be an argument" for bringing all of these together into a single institution that would operate as a 'one-stop shop', thereby bringing increased simplicity. He added that "the review we are conducting will look at both options".[177]

148. **Some witnesses identified potential benefits in having a single institution that would operate as a 'one-stop shop' for public**

175 Q 33
176 Q 15
177 Q 82

financing, as is currently the case in some EU Member States. More evidence is needed about the synergies that could be gained from this approach, and we therefore welcome the Government's commitment to look at this issue as part of its ongoing review. As part of this, it should also consider ways in which such an institution could reflect the interests of the regions and the devolved administrations in its governance structure.

SUMMARY OF CONCLUSIONS AND RECOMMENDATIONS

The EIB and its activities in the UK

1. The EIB has been an important provider of funding for the UK, including almost €50 billion over the last decade. This has included the financing of key projects in areas such as energy and the environment, transport, water and sewerage, education and housing. The EIF has also been an important investor in UK venture capital, growth and mid-market funds, facilitating access to finance for SMEs. As the UK will lose access to these important sources of finance, there will be negative consequences for future projects in these areas unless alternative sources are established. (Paragraph 23)

2. The availability of cheaper, long-term financing from the EIB is one of its key benefits. Losing access to the EIB would almost certainly increase the cost of capital in different sectors of the UK economy and could mean that some future projects would no longer be commercially viable. Similarly, if the EIF withdraws from the UK market, small businesses may find it more difficult to access affordable finance. If access to the EIB and EIF is lost as a result of Brexit, the Government will need to ensure that comparable funding continues to be available. (Paragraph 33)

3. The independent expertise and high-quality due diligence of the EIB and EIF are essential for crowding in private investment. Their participation in specific projects provides a stamp of approval and a positive signal to the market, thereby encouraging additional investment from the private sector. If these institutions stop supporting projects in the UK after Brexit, the Government must ensure that means to replicate their independent expertise and due diligence continue to be available. (Paragraph 41)

The impact of Brexit on the UK's relationship with the EIB

4. There was a marked decline in funding from the EIB and EIF after the referendum and triggering of Article 50, which appears to go beyond what could be explained by the increased due diligence for UK projects. The scale of this decline suggests that there may be financing gap in the UK for projects that have previously benefited from investment by the EIB and EIF. (Paragraph 51)

5. For ongoing projects, we recognise that the Withdrawal Agreement safeguards existing loans as well as those approved but not made prior to Brexit. If the Agreement is not approved, the Government notes that existing UK projects should be protected through section 4 of the EU Withdrawal Act 2018 and that affected organisations do not need to take any action in this regard. We are however disappointed that this announcement was made on 10 January, with only 78 days until Brexit, and gave no indication about possible replacements for EIB funding. (Paragraph 52)

6. Under the Withdrawal Agreement, the UK will receive the capital it has paid in to the EIB but not any share of the profit, as reflected in the retained earnings, nor any interest or dividends for the 12-year period over which the capital will be repaid. While we recognise that this was part of a complex and wide-ranging negotiation on the financial settlement, and that the EIB's statute is silent on the issue, we regret that the Government failed to provide a cogent explanation of the rationale for the position taken in the negotiations. Given the substantial amounts of money potentially involved—representing

up to 20 percent of the UK's obligations under the financial settlement—we call on the Government to explain in clear terms why it did not press for the EIB's profitability to be taken into account in the final calculation of the financial settlement. (Paragraph 56)

7. Article 308 TFEU clearly states that only EU Member States can be members of the EIB. Continued UK membership of the EIB would therefore require a change to the EU Treaties, making it highly unlikely. Our figures show that the EIB's activity in the UK has already fallen by 87 percent since 2016, and by 91 percent for the EIF. At this late stage in the process of the UK's withdrawal from the EU, we are concerned that the Government has said so little about the UK's future relationship with the EIB and disappointed by its lack of ambition in this regard. (Paragraph 64)

8. The starting point of any future relationship is that the UK will be a third country. While existing EIB agreements with third countries—notably the states of the European Free Trade Association (EFTA)—provide precedents, the Government should also urgently explore options for a deeper bilateral relationship. Concluding a third country agreement should be an immediate priority, to enable some EIB lending to continue, albeit at a reduced level, as a temporary measure. (Paragraph 65)

The consequences of losing access to the EIB

9. The loss of EIB funding after March 2019 will have different effects on different sectors of the economy. Utilities such as water and sewerage may be able readily to access alternative sources of finance, albeit at an increased cost. More innovative projects, or those that fall within the EIB's broader social mandate, may struggle to raise money in the private sector. As part of its ongoing infrastructure finance review, the Government should identify the sectors most exposed to losing EIB access as well as issues related to SMEs' access to finance from the EIF. (Paragraph 75)

10. In the short term, the Government should take urgent measures to minimise any financing gap for UK infrastructure. This could include extending the UK Guarantees Scheme to projects that may not meet the current threshold of being 'nationally significant' and allowing it to offer different financing options, given its low take up. The Government should consult with affected industries on how the UK Guarantees Scheme could be improved, with a view to incorporating changes to the Scheme in its forthcoming National Infrastructure Strategy. (Paragraph 82)

11. We welcome the fact that the Government has already announced changes to the resources of the British Business Bank (BBB) as well as its commitment to providing it with additional funding when the UK loses access to the EIF. The BBB told us that it is increasingly acting as a cornerstone investor that crowds in private investment, but this view did not appear to be shared by some industry stakeholders. Greater efforts to demonstrate that it is available to fulfil the functions of enhanced due diligence and acting as a cornerstone investor may be required and the BBB should make clear how it measures success in this regard. (Paragraph 91)

Establishing a UK infrastructure bank

12. Several witnesses proposed establishing a UK infrastructure bank, if access to the EIB is lost. We note that the National Infrastructure Commission

has called for such an institution to be established by 2021. In responding to the NIC's recommendation as part of its infrastructure finance review, the Government should urgently identify and consult on potential market failures in the UK infrastructure market, particularly in areas where the EIB has previously operated. The Government should then explain how it intends to address any market failures, considering in this light the role that could be played by a UK infrastructure bank. (Paragraph 102)

13. There could be significant benefits to having an infrastructure institution that is independent from Government, particularly with respect to individual investment decisions, thereby generating greater confidence from investors, particularly for long-term projects, and crowding in investment from the private sector. Such an institution would need to be free from day-to-day political interests, though should be aligned with clearly defined strategic national priorities. (Paragraph 109)

14. As part of its infrastructure finance review, the Government should clearly identify the areas where an independent infrastructure institution could deliver benefits, particularly given any loss of access to the EIB. Depending on the results of its review, we urge the Government to consult on the establishment of an independent UK infrastructure bank as part of its National Infrastructure Strategy. (Paragraph 110)

15. Witnesses underlined the importance of having sufficient expertise within any national infrastructure institution, enabling it to conduct credible due diligence and be able to give a clear 'stamp of approval' for infrastructure projects. This would give confidence to private investors in the market and thereby crowd in additional investment. Attracting such expertise may be easier for an independent institution than for the Government itself. We urge the Government to take this issue into account as part of its infrastructure finance review and National Infrastructure Strategy. (Paragraph 115)

16. One argument for an independent institution is its potential to play a countercyclical role in the event of an economic downturn, during which it could continue to support long-term infrastructure finance and contribute towards the UK's economic recovery. This potential benefit should be recognised as part of the Government's ongoing work in this area. (Paragraph 119)

17. If the Government decided to establish a UK infrastructure bank, our future relationship with the EU may require us to respect EU State aid rules when considering its design. This was the case for the Green Investment Bank and continues to set the limits of the British Business Bank's activities. However, the example of some Member States, notably Germany, shows that these rules allow sufficient flexibility to enable the creation of such a national infrastructure institution. (Paragraph 126)

18. The EIB's liabilities do not feature on the national balance sheets of EU Member States, but we were told that a similar UK institution would almost certainly feature within the Government's measure of public sector net debt. While such an institution would also have assets and would probably be able to fund the interest on its paid-in capital, this could have significant implications for the Government's commitment to reduce public debt as a proportion of GDP. (Paragraph 133)

19. The measure of Government debt does not fall within the scope of this inquiry. While we acknowledge that it is for the Government to choose the best way to calculate public sector debt, such accounting decisions should not determine economic decisions about the optimal form of support for long-term infrastructure investment in the UK. (Paragraph 134)

20. The EIB finances itself on the capital markets, on the basis of a guarantee by EU Member States. This could serve as a possible model for a UK infrastructure bank. While it would almost certainly have higher borrowing costs than the Government itself, there may be compensating benefits. We therefore invite the Government, in considering a UK infrastructure bank, to take into account the advantages and disadvantages of such an institution funding itself on the capital markets. (Paragraph 141)

21. Some witnesses identified potential benefits in having a single institution that would operate as a 'one-stop shop' for public financing, as is currently the case in some EU Member States. More evidence is needed about the synergies that could be gained from this approach, and we therefore welcome the Government's commitment to look at this issue as part of its ongoing review. As part of this, it should also consider ways in which such an institution could reflect the interests of the regions and the devolved administrations in its governance structure. (Paragraph 148)

APPENDIX 1: LIST OF MEMBERS AND DECLARATIONS OF INTEREST

Members

Lord Bruce of Bennachie
Lord Butler of Brockwell
Lord Cavendish of Furness
Lord De Mauley (until 15 January 2019)
Lord Desai
Baroness Falkner of Margravine (Chairman)
Lord Giddens
Baroness Liddell of Coatdyke
The Earl of Lindsay
Baroness Neville-Rolfe
Lord Thomas of Cwmgiedd
Viscount Trenchard (from 15 January 2019)
Lord Vaux of Harrowden

Declarations of interest

Lord Bruce of Bennachie
No relevant interests
Lord Butler of Brockwell
Adviser to TT International Asset Management
Lord Cavendish of Furness
No relevant interests
Lord De Mauley (until 15 January 2019)
No relevant interests
Lord Desai
No relevant interests
Baroness Falkner of Margravine (Chairman)
No relevant interests
Lord Giddens
No relevant interests
Baroness Liddell of Coatdyke
External Adviser, PwC
The Earl of Lindsay
No relevant interests
Baroness Neville-Rolfe
Commercial Secretary to HMT 2016–2017
Secure Trust Bank Plc, Capita Plc, Non-Executive Director 2017–
Lord Thomas of Cwmgiedd
No relevant interests
The Viscount Trenchard (from 15 January 2019)
No relevant interests
Lord Vaux of Harrowden
No relevant interests

The following Members of the European Union Select Committee attended the meeting at which the report was approved:

Lord Boswell of Aynho (Chairman)
Baroness Armstrong of Hill Top
Baroness Brown of Cambridge
Lord Cromwell
Baroness Falkner of Margravin
Lord Jay of Ewelme
Baroness Kennedy of The Shaws
The Earl of Kinnoull
Lord Liddle
Baroness Neville-Rolfe
Baroness Noakes
Lord Polak
Lord Ricketts
Lord Risby
Lord Soley
Baroness Suttie
Baroness Verma
Lord Whitty

During consideration of the report the following members declared an interest:

Baroness Brown of Cambridge

Vice Chancellor of Aston University 2006–2016 during which time the University received an EIB loan

Former NED of Green Investment Bank

Sector Champion for Offshore Wind Sector Deal

NED of Offshore Renewable Energy Catapult

Baroness Noakes

Director, Royal Bank of Scotland Group Plc

Interests in wide range of listed shares, as shown in Register of Members' Interests, including companies which have an interest in infrastructure investment

Lord Ricketts

Non-Executive Director, Group Engie, France

Strategic Adviser, Lockheed Martin UK

A full list of Members' interests can be found in the Register of Lords Interests: http://www.parliament.uk/mps-lords-and-offices/standards-and-interests/register-of-lords-interests/

APPENDIX 2: LIST OF WITNESSES

Evidence is published online at https://www.parliament.uk/brexit-european-investment-bank-lords-inquiry and available for inspection at the Parliamentary Archives (020 7219 3074).

Evidence received by the Committee is listed below in chronological order or oral evidence and in alphabetical order. Those witnesses marked with ** gave both oral evidence and written evidence. Those marked with * gave oral evidence and did not submit any written evidence. All other witnesses submitted written evidence only.

Oral evidence in chronological order

**	Phil Graham, Chief Executive, National Infrastructure Commission	QQ 1–19
**	James Richardson, Chief Economist, National Infrastructure Commission	QQ 1–19
**	Peter Clutton-Brock, Policy Adviser, E3G	QQ 20–29
*	Alex Conway, Assistant Director, Brexit and European Programmes, Greater London Authority	QQ 20–29
*	Philip Harding, Director of Finance and Business Affairs, University College London	QQ 20–29
*	Piers Williamson, Chief Executive, The Housing Finance Corporation	QQ 20–29
*	Laurie Macfarlane, Public Banking Lead, UCL Institute for Innovation and Public Purpose	QQ 30–41
*	Josh Ryan-Collins, Head of Research, UCL Institute for Innovation and Public Purpose	QQ 30–41
*	Giles Derrington, Head of Policy, techUK	QQ 42–54
**	Tim Hames, Director General, British Private Equity and Venture Capital Association	QQ 42–54
*	Victoria Roberts, Head of Government Affairs and Policy, Innovate Finance	QQ 42–54
*	Catherine Lewis La Torre, Chief Executive Officer, BBB Patient Capital Holdings	QQ 55–64
**	Keith Morgan, Chief Executive Officer, British Business Bank	QQ 55–64
*	Eva Witt, Director of Federal and European Affairs, KfW	QQ 65–75
*	Robert Jenrick MP, Exchequer Secretary to the Treasury	QQ 76–88
*	David Lunn, Director of EU Exit, HM Treasury	QQ 76–88
*	Philip Duffy, Director for Growth and Enterprise, HM Treasury	QQ 76–88

Alphabetical list of all witnesses

	Anglian Water Services	EIB0005
	British Business Bank	EIB0015
	British Private Equity and Venture Capital Association (BVCA)	EIB0009
**	Peter Clutton-Brock, Policy Adviser, E3G (QQ 20–29)	
*	Alex Conway, Assistant Director, Brexit and European Programmes, Greater London Authority (QQ 20–29)	
*	Philip Duffy, Director for Growth and Enterprise, HM Treasury (QQ 76–88)	
	E3G	EIB0013
	East of England European Partnership	EIB0006
	Energy UK	EIB0011
	The Infrastructure Forum	EIB0007
**	Phil Graham, Chief Executive, National Infrastructure Commission (QQ 1–19)	EIB0014
**	Tim Hames, Director General, British Private Equity and Venture Capital Association (BVCA) (QQ 42–52)	
*	Philip Harding, Director of Finance and Business Affairs, University College London (QQ 20–29)	
*	Robert Jenrick MP, Exchequer Secretary to the Treasury, HM Treasury (QQ 76–88)	
*	David Lunn, Director, EU Exit, HM Treasury (QQ 76–88)	
*	Catherine Lewis La Torre, Chief Executive Officer, BBB Patient Capital Holdings (QQ 55–64)	
*	Laurie Macfarlane, Public Banking Lead, UCL Institute for Innovation and Public Purpose (QQ 30–41)	
**	Keith Morgan, Chief Executive Officer, British Business Bank (QQ 55–64)	EIB0015
	National Infrastructure Commission	EIB0014
**	James Richardson, Chief Economist, National Infrastructure Commission (QQ 1–19)	
*	Victoria Roberts, Head of Government Affairs and Policy, Innovate Finance (QQ 42–52)	
*	Josh Ryan-Collins, Head of Research, UCL Institute for Innovation and Public Purpose (QQ 30–41)	
	Scottish Government	EIB0010
	Unite the Union	EIB0012
	Universities UK	EIB0008

	Welsh Government	EIB0004
*	Piers Williamson, Chief Executive, The Housing Finance Corporation (QQ 20–29)	
*	Eva Witt, Director of Federal and European Affairs, KfW (QQ 65–75)	

APPENDIX 3: CALL FOR EVIDENCE

The House of Lords EU Financial Affairs Sub-Committee, chaired by Baroness Falkner of Margravine, has launched an inquiry into the UK's future relationship with the European Investment Bank (EIB) and the potential consequences of the UK's losing access to EIB funding. The Committee invites interested individuals and organisations to submit evidence to this inquiry.

Written evidence is sought by 14 September 2018. Public hearings are expected to take place September to November. The Committee aims to report to the House in December. The report will receive a response from the Government and will be debated in the House.

Background

The EIB is the largest multilateral lender in the world. The UK is currently a member of the EIB and benefits substantially from this membership. It is also a beneficiary of the European Investment Fund (EIF), of which the EIB is the majority shareholder. Many sectors in the UK secure funding from these institutions: the EIB funds social housing; schools, colleges and universities; and infrastructure projects (e.g. water and transport); and the EIF funds many SMEs and FinTech firms through the UK's venture capital sector.

The proposed Withdrawal Agreement includes a commitment to a repayment of the UK's paid-in capital. As set out in Treaty on the Functioning of the European Union, the members of the EIB are the Member States of the EU. Without a change to the Treaty, the UK will therefore cease to be a member of the EIB and would only be eligible to receive EIB loans if it was awarded 'partner' status.

The Committee will consider the options for future participation in the EIB or EIF and for any UK alternatives. The UK currently has no national promotional bank, as some Member States do. The British Business Bank, as currently configured, supports predominantly small to medium-sized enterprises. Despite the recent increase of £400 million in its available funds, this is dwarfed by the £5.6 billion that the UK received from the EIB in 2015, supporting some £16 billion of overall investment. The Committee seeks evidence on whether the remit of the British Business Bank should be expanded to include either or both of the infrastructure and venture capital funding currently provided by the EIB and EIF, as well as on other options for financing.

Although the UK is a member of the EIB until Brexit and still eligible for EIB funding, there is evidence of a decline in funding to the UK. Whatever the future relationship with the EIB and whatever alternatives the Government might put in place in response to any loss of EIB or EIF funding, this decline has immediate effects. The Committee will therefore also explore what short-term actions might be required to support those businesses who are already being negatively affected by this loss.

The inquiry

The Committee seeks evidence on the following questions in particular:

(1) How reliant on EIB funding are UK firms? Are there particular sectors that will be more affected by any loss of EIB funding?

(2) How dependent is the UK SME sector on EIF financing? Are there particular sectors that will be more affected by any loss of EIF funding (e.g. FinTech)?

(3) How reliant is the UK's venture capital sector on EIB and EIF funding? How much funding from other sources is contingent on that EIB or EIF funding? Will UK venture capital funds face any challenges in securing funding elsewhere in the absence of EIF funding?

(4) How has the future withdrawal of the UK affected the ease of securing affordable finance? Have firms noticed any difficulties in securing EIB funding or the length of time it takes to do so?

(5) What options are there for future participation in the EIB's lending programmes? Should the UK attempt to secure a change to the EIB's statute to allow UK membership and how likely would it be to succeed? Could the UK secure 'partner' status?

(6) Are there options for the UK's future participation in the EIF, or should the Government focus on the Investment Fund to be incubated by the British Business Bank?

(7) What difference has the additional £400 million available to the British Business Bank made to funding opportunities for the UK's venture capital industry?

(8) How should the UK support those sectors who may lose EIB funding post-Brexit? Should the UK create a national promotional bank, expand the remit of the British Business Bank to include larger businesses, or develop alternative sources of finance for affected sectors?

(9) What lessons from the performance of the EIB might the UK learn if it were to try to step into any gap in EIB funding?

(10) If the UK were to develop alternative sources of finance, how long might it take to do so? Would it be necessary to implement short- to medium-term alternatives in the interim?

You need not address all of these questions.