



EUROPEAN COMMISSION

## MEMO

Brussels, 27 March 2014

# Communication on long-term financing of the European economy: frequently asked questions

See also [IP/14/320](#)

## 1. What is long-term financing?

There is no strict definition of long-term financing. It can be defined through its key features:

- It finances *productive* activities which support growth by reducing costs, diversifying means of production and creating jobs in a sustainable and inclusive way.
- It is *patient*, in that investors take into account the long-term performance and risks of their investments, rather than short-term price fluctuations. Investors are generally expected to hold an asset for a long or indefinite period of time. This long-term perspective acts in a counter-cyclical manner and promotes financial stability.
- It is *engaged*, in that investors take longer-term aspects such as environmental, social and governance issues into account in their investment strategies. This sustained and direct engagement from investors ensures better alignment of incentives with longer term interests throughout the investment chain.

## 2. How is long-term financing different to long-term investment?

Long-term investment represents investment that enhances the *productive* capacity of the economy and drives sustainable growth and competitiveness. This includes investment in energy, transport and communication infrastructures that respond to Europe's needs, as well as in Small and Medium Enterprises (SMEs), education and research and development. Europe faces large-scale long-term investment needs, which are crucial to support sustainable growth. Investment needs for transport, energy and telecom infrastructure networks of EU importance alone are estimated at €1 trillion for the period up to 2020 as identified by the [Connecting Europe Facility](#). Significant investment will also be needed in human capital and in R&D, new technologies and innovation under the [Europe 2020 strategy](#) and the [2030 climate and energy package](#).

Long-term financing represents the financing of such long-term investment in a "patient" and "engaged" way, as described above.

## 3. Why is there a need to address long-term financing?

The economic and financial crisis has affected the ability of the EU financial sector to channel funds to the real economy, in particular to long-term investment. Heavy dependence on bank intermediation, combined with bank deleveraging and reduced investor confidence, has reduced funding to the economy.

The European Union has acted with determination to reverse these trends and restore the conditions for sustainable growth and investment. Public finances have been consolidated and procedures for better coordination of budgetary and economic policies have been put in place ([MEMO/13/979](#)). The [European Central Bank \(ECB\)](#) has acted firmly to restore confidence in the markets, and the establishment of the Banking Union ([MEMO/14/57](#)) is helping to reduce financial fragmentation and restore trust in the euro area.

Harnessing these improvements requires long-term investment which can underpin sustainable and balanced growth. The ability of the financial system to channel funds to long-term investments will be key to securing Europe's position on a sustainable growth path.

The role of non-bank financing will also be essential in this respect. While banks will continue to play a significant role, the diversification of funding to include more capital markets-based financing is important in the short-run, to improve the availability of financing, as well as in the long-run, to help the European economy sustain any future crises better.

#### **4. Why is the Commission adopting a Communication on long term financing now?**

Following the outbreak of the financial crisis in 2008 and in line with the commitments agreed with the EU's G20 partners, the immediate EU priority has been the stabilisation of financial markets. Financial sector reform has been a crucial instrument in achieving that.

The EU is currently witnessing the first signs of recovery: according to the winter 2014 economic forecast ([IP/14/118](#)), economic growth is expected to reach around 1.5% in the EU in 2014, before reaching 2% in 2015.

Efforts are needed to secure Europe's position on a sustainable growth path, including by unlocking all possible means of finance of the economy. It is an ambitious and complex task, which the European Commission set out to do with the [2011 Action Plan to improve SMEs' access to finance](#) ([IP/11/1513](#)) and the [2013 Green Paper on long-term financing](#) ([IP/13/274](#))

This Communication builds on the 2013 Green Paper and on the ensuing public consultation and takes into account other initiatives in this area by the Economic and Financial Committee and the European Parliament, as well as by our international partners within G20 and OECD. It sets out a comprehensive framework to pull together all the various measures needed.

## 5. Are proposals legislative?

Some of the actions proposed are of a legislative nature. Besides the proposed new rules on IORPs adopted today, these include:

- a review of the **Shareholders' Rights Directive** to increase shareholder engagement
- a Recommendation aimed at improving the quality of **corporate governance** reporting.

Both these proposals are due to be presented by the Commission in the coming weeks. Other actions relate to the ongoing calibration of the regulatory framework to ensure that it most effectively enables the financial sector to support the real economy, without jeopardising financial stability. For example:

- for **banks**, finalising the delegated acts on the Liquidity Cover Ratio (a liquidity ratio with a one-month horizon) and the Net Stable Funding Ratio (a liquidity ratio with a one-year horizon) – see [MEMO/13/690](#) on Capital Requirements Directive IV;
- for **insurers**, finalising the delegated acts under Solvency II, in particular with respect to the calibration of capital requirements; and
- considering ways to revive sustainable **securitisation markets**, with due consideration to the risks as well as to the differentiated nature of such products. Securitisation transactions enable banks to refinance loans by pooling individual assets and converting them into securities that are attractive to institutional investors. For institutional investors, such securities, if of sufficient size, offer liquid investment opportunities in asset classes in which they do not invest directly, e.g. SMEs or mortgages. From a bank's perspective, such transactions unlock capital resources by allowing banks to reduce their regulatory capital requirements, thus increasing their ability to expand their lending and finance economic growth. Some securitisation markets have been at the heart of the financial crisis in 2007/2008, leading to a significant overhaul of their regulatory treatment. Defining criteria for identifying safe, high-quality securitisation structures and products and distinguish them from the securitisation structures that played a negative role in the crisis is an important first step, which the Commission and the international standard setters have already started to work on. A wider use of high quality securitisation products, with appropriate mitigation of risks involved, has the potential to unlock additional funding to the real economy.

Other actions are of a more exploratory nature and will require further analysis to assess the best ways to:

- mobilise more **personal pension savings** and **private savings** for long-term financing;
- make better use of **public finance**, including state-backed National Promotional Banks and export credit agencies, to maximise the return on public investment and the leverage that investment spending can give to growth;
- develop **European capital markets** further, for equity as well as for corporate bonds, to ensure a more diversified financing of the European economy;
- improve **SMEs' access to finance** by improving credit information on SMEs and helping SMEs access capital markets;
- attract **more private finance to infrastructure** by making more information available on the credit history of infrastructure loans and on infrastructure investment plans;
- develop the overall environment for investment, by exploring a number of **cross-cutting issues**, including corporate governance, accounting, tax and legal issues.

## **6. Why is there a particular focus on infrastructure and SMEs?**

Infrastructure and SMEs are key contributors to sustainable growth. High quality infrastructure improves the productivity of the rest of the economy, enabling growth, and facilitates the interconnection of the single market. Investment needs for transport, energy and telecom infrastructure networks of EU importance are estimated at €1 trillion for the period up to 2020. Significant investment will also be needed in R&D, new technologies and innovation as set out in the [Europe 2020 strategy](#) and the [2030 climate and energy package](#).

SMEs represent around two-thirds of employment and nearly 60% of the value added in the EU. They contribute significantly to GDP growth through their overall importance as well as their ability to innovate, grow and create employment.

The funding of both infrastructure and SMEs has been particularly affected by the crisis. For example, SMEs are particularly dependent on local bank finance and therefore the banking crisis has deeply affected their access to funds. While the situation is slowly improving, it is still the case that only 33% of SMEs that apply for credit in Greece receive the full amount and only 50% do so in Spain and Italy (compared to a 65% average in the euro area and 87% in Germany).

## **7. How does the Communication fit in with work at European and international level?**

Since the launch of the debate by the Commission with the publication of the Green Paper on long term financing in March 2013 ([IP/13/274](#)), the debate on long-term financing has been echoed at European and international level. The Economic and Financial Committee set up a High Level Expert Group, which published its [report in December 2013](#), focused on SMEs and infrastructure. The European Parliament adopted on 26 February 2014 its own initiative [report on the long-term financing of the European economy](#). The report includes many of the issues covered by this Communication.

At international level, in September 2013 the G20 endorsed a work plan on financing for investment and established a working group to carry out further work on long-term finance. The OECD has developed high-level principles for institutional investors when engaging in long-term financing and has a task force continuing to work on these issues.

## **8. What preparatory work has been done?**

The European Commission adopted on [25 March 2013 a Green Paper on the long-term financing of the European economy](#), which initiated a broad debate on the different factors that drive the ability of the European economy to attract the funds it needs to sustain and accelerate its recovery. The paper aimed to explore how the savings of governments, corporates and households can be better channelled to long term investment needs and how the financing of long-term investment in Europe can be developed and diversified.

The Green Paper consultation drew 292 responses from all segments of the economy. It was very positively received by stakeholders, who welcomed in particular the Commission's initiative in launching and framing this timely debate. A large majority of stakeholders agreed with the need to broaden the sources of long-term financing in Europe, while recognising the important role that banks will continue to play, particularly for SMEs. While a well-defined and stable regulatory environment was underlined as very important, many stakeholders also called for better calibration of regulatory reform to take account of long-term financing objectives.

**For more information:**

[http://ec.europa.eu/internal\\_market/finances/financing-growth/long-term/index\\_en.htm](http://ec.europa.eu/internal_market/finances/financing-growth/long-term/index_en.htm)

ANNEX: Table of actions

	Area	Action	Date
1	<b>Banks</b>	Reports on the appropriateness of the Capital Requirements Regulation (CRR) requirements in relation to long-term financing.	2014, 2015
		Delegated Act on Liquidity Coverage Ratios (LCR), final calibration of the Net Stable Funding Ratio (NSFR) and monitoring period for the CRR new liquidity rules to take full account of long term financing needs.	H1 2014 (for LCR DA)
2	<b>Insurance companies</b>	Delegated Act for Solvency II to include a number of incentives to stimulate long-term investment by insurers.	H2 2014
3	<b>Pension funds</b>	Call for Advice to the European Insurance and Occupational Pensions Authority (EIOPA) with the objective of creating a single market for personal pensions and thus potentially mobilising more personal pension savings for long-term financing.	H2 2014
4	<b>Private savings account</b>	Study of possible market failures and other shortcomings regarding cross-border flows of savings, including an overview of national savings account models and an assessment of the advantages of introducing an EU savings account.	By end 2014
5	<b>National promotional banks</b>	Communication regarding promotional banks to provide guidance on general principles, governance and transparency, supervision and regulatory aspects, and the role of national promotional banks (NPBs) in co-investing and delivering EU budget funds.	By end 2014
		Cooperation of NPBs with the EIB/EIF and possibly other multilateral development banks (MDBs) to be encouraged and monitored. Report to the December 2014 European Council.	By end 2014
6	<b>Export Credit Agencies</b>	Report on promoting better coordination and cooperation among existing national credit export schemes.	-
7	<b>Equity and corporate bond markets</b>	Delegated Act for MiFID 2 on SME growth markets to minimise the administrative burden for issuers on these markets, while maintaining high levels of investor protection.	-
		Study on whether, following the introduction of MiFID 2, further measures are necessary to enable the creation of a liquid and transparent secondary market for corporate bonds.	-
		Assessment of the implications and effects of the rules of the Prospectus Directive.	By end 2015
		Assessment of the eligibility criteria for investments by UCITS regarding securities listed on SME growth markets.	-
8	<b>Securitisation</b>	Differentiation of "high" quality securitisation products across financial sectors and possible preferential regulatory treatment compatible with prudential principles.	Ongoing

	Area	Action	Date
		Global standards on securitisation, in particular on risk retention, high quality standardisation and transparency to ensure consistency and avoid regulatory arbitrage.	Ongoing
9	<b>Covered bonds</b>	Review of the covered bond treatment in the CRR with a view to building the basis for an integrated European covered bond market.	By end 2014
		Study on the merits of introducing an EU framework for covered bonds.	-
10	<b>Private placement</b>	Study to map out the private placement markets in Europe against other locations/practices, analyse their key success drivers and develop policy recommendations on how this success can be replicated more widely in the EU.	By end 2014
11	<b>Improving SMEs access to finance</b>	Mapping of the EU and national legislation and practices affecting the availability of SME credit information, with a view to considering possible EU approaches to the credit scoring industry and assessing the feasibility of harmonising/increasing the comparability of SME data across the EU.	2014
		Revival of the dialogue between banks and SMEs particularly with regards to feedback provided by banks on loan applications and assessment of best practices on helping SMEs to access capital markets.	Ongoing
12	<b>Attracting private finance to infrastructure</b>	Evaluation of the feasibility of voluntarily making available existing information on infrastructure investment plans and projects by national, regional and municipal authorities.	2014
		Evaluation of the feasibility and practical arrangements of collecting and, where possible, making available comprehensive credit statistics on infrastructure loans and of setting up a single-point compilation of project bond issue data.	2014
13	<b>Corporate governance</b>	Proposal for the revision of the Shareholder Rights Directive to better align long-term interests of institutional investors, asset managers and companies.	H1 2014
		Assessment of employee stock option (ESO) across the EU with a view to identifying problems with cross-border implementation of employee financial participation (EFP)/ESO schemes and formulating possible EU actions to promote EFP and ESO.	2014
		Recommendation aimed at improving the quality of corporate governance reporting; report on possible additional transparency initiatives to incentivise institutional investors and asset managers to take better account of environmental, social and governance (ESG) issues; study on fiduciary duties and sustainability.	2014
14	<b>Accounting standards</b>	Evaluation of the appropriateness of the use of fair value within the endorsement process of the revised International Financial Reporting Standards (IFRS).	-

	Area	Action	Date
		Invitation to the International Accounting Standards Board (IASB) to give due consideration to the effect of its decisions on the investment horizons of investors.	-
		Evaluation of the IAS Regulation to explore the appropriateness of the endorsement criteria, taking account of Europe's long-term financing needs.	2014
		Public consultation to examine (i) the case for a simplified accounting standard for the consolidated financial statements of listed SMEs, and (ii) the usefulness of a complete self-standing accounting standard for non-listed SMEs to supplement the Accounting Directive.	2014
<b>15</b>	<b>Tax and legal environment</b>	Monitoring of the implementation of measures by Member States and to issue country-specific recommendations where necessary to reduce the tax bias for debt vs. equity in the Annual Growth Surveys and the European Semester process.	Ongoing
		Review of the implementation of the March 2014 Recommendation on best practice principles to enable the early restructuring of viable enterprises and to allow bankrupt entrepreneurs to have a second chance and assessment of possible additional measures.	2014
		Report on the law applicable to third party aspects of the assignment of claims.	2014