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Staying the course: The EIB's reluctant COVID-19 response

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Key Points

- The EIB's response to the COVID-19 crisis consisted only of small changes to its existing operations, both regarding its total lending and lending to the health sector.
- Through the European Guarantee Fund, the EIB mobilised €187 billion of additional investments.
- To protect its credit rating, the Bank eschewed riskier operations and sought financial guarantees.
- The EIB's reliance on the financial sector to transmit its policy had drawbacks both for the control of the use of funds and for transparency.
- Whereas other EU institutions implemented significant new policies in response to the pandemic, the EIB's business model limited the Bank's ability to adapt to an unprecedented shock.

Introduction

The European Investment Bank (EIB) was a central actor in formulating the EU's response to the COVID-19 pandemic. It aimed 'to contain the economic effects of the crisis and tackle immediate health-related emergencies' (European Investment Bank, 2021, p. 13). The EIB itself claims success in supporting SMEs during and after the lockdown and in co-funding the development of vaccines. However, as David Howarth and Helen Kavvadia of the University of Luxembourg argue in a working paper (Howarth & Kavvadia, 2022), the EIB's response fell short of the public's needs and did not amount to a comprehensive repositioning of the Bank. The EIB's inability to change tack at the onset of the pandemic indicates how the Bank's ability to serve the public has been constrained by its business model.

The EIB's COVID-19 measures

The EIB's response to the COVID-19 crisis centred on two decisions taken in the spring of 2020. The first round of measures consisted of re-purposing existing lending programmes in an immediate response package of €28 billion that served as 'bridge loans or top-ups to existing EIB and European Investment Fund (EIF) operations' (European Investment Bank Group 2022, p 2). Since the start of the pandemic, the EIB and EIF have approved €72 billion in targeted support to businesses, public health, and vaccine distribution (European Investment Bank, 2021, p. 13).

The European Guarantee Fund (EGF), agreed in June 2020, was the second pillar of the EIB's COVID response. Under the EGF, the EIB and the EIF backstop commercial and promotional banks' lending to enterprises. The

EGF has a volume of €24.4 billion (provided by 22 EU Member States; five declined to participate), which the EIB uses to leverage greater volumes of private lending. In mid-2022, the EIB expected to mobilise investments of €187.4 billion, against a target of €200 billion.[1]

Yet, these shifts amount only to a limited change in the EIB's overall activities as the change in its lending activity between 2018/19 and 2020/21 shows. Its total lending activity increased only modestly to €125 billion in the years of the COVID-19 crisis from €118 billion in the two preceding years. Despite pressure from the European Council to boost support to the health sector, the EIB in 2020/21 invested just €7.7 billion in that field, which represented 6% of its overall lending and an additional effort of a mere €3 billion.

In sum, though the EIB passed several measures during the COVID crisis, these neither responded to the exigencies of the public health crisis nor did they amount to a large economic stimulus.

Explaining the EIB's limited response

Compared to other initiatives at the EU level, such as the introduction of common large-scale borrowing under Next Generation EU, the EIB's COVID-19 response did not represent a radical departure from its established way of doing business. Indeed, the EIB's actions can be understood as being constrained by prior institutional choices.

One cornerstone of the EIB's business model is the Bank's prized AAA credit rating. To maintain it, the bank pursues a very conservative lending policy and seeks guarantees from its shareholders before engaging in riskier operations. The EIB has sought direct risk coverage of the kind that the EGF provided since the 1960s (although the EGF was the first case where such guarantees came from the Member States directly, rather than EU budgetary resources).

The EIB's caution has contributed to its financial success: the Bank has remained profitable and maintained its credit rating throughout the COVID-19 crisis. However, this prudence has also limited the EIB's ability to assume greater risks when that would have been in the public interest.

A second important factor is the EIB's evolving business model. Over the past decade, the EIB has shifted from policy-based banking towards fee-based banking services where it manages third-party funds (Kavvadia, 2020). The EIB has sought to take riskier operations, not least lending to SMEs, off its balance sheet by relying on its subsidiary, the European Investment Fund (Cooiman, 2021). Even though the EIF's balance sheet amounts only to a fraction of the EIB's, the Fund has provided the majority of the operations under the EGF and assumed greater risks (Counter Balance, 2022).

The EIB has also increasingly resorted to intermediated lending, that is, the provision of credit lines to financial institutions that are then on-lent to the ultimate recipients. Intermediated lending has allowed it to scale up lending through so-called global loans, but this instrument has arguably come at the cost of limited control and transparency regarding the use of the funds. Besides, since intermediated lending primarily relieved the intermediary banks' liquidity and capital constraints, arguably it has been the banking system, rather than SMEs, that has gained most from the EGF (Clifton et al., 2020).

The EIB's low risk appetite and its lengthy approval procedures have, lastly, also limited its ability to ramp up riskier health sector investments at short notice. Granted, the EIB has used several instruments to fund the health sector, including a joint facility with the European Commission. However, only one out of fourteen projects was dedicated to stopping COVID-19. Some projects had already been approved before the pandemic (Clifton et al., 2020). Even if the EIB's decision to fund non-fixed assets represented an innovation in its lending decisions, it once again insisted on de-risking these investments through EU funds.

[1] Source: European Guarantee Fund.

The EIB's COVID-19 response thus represents mostly a continuation of its previous policies. While these policies allowed the Bank to scale up its conventional lending instruments, the EIB offered few new policies to support the efforts of containing the pandemic.

Outlook

The COVID-19 pandemic has provided a window of opportunity for several breakthroughs in the EU's economic governance. The EIB, however, deviated only to a small extent from previous policies, above all its conservative lending policy and its reliance on financial intermediaries. This approach has allowed the EIB to preserve its credit rating and relieve pressures on the financial sector, but its contribution to resolving the health crisis was limited.

The conflicts between public banks' policy roles (which require risk-taking) and their business model (which mandates prudence) are, of course, well-known (Clifton, Díaz-Fuentes, & Howarth, 2021). Nonetheless, going forward, the EIB's handling of the COVID-19 crisis raises questions about what it would take to enable the Bank to act in the public interest in future contingencies. In this regard, the EIB's limited risk appetite, its increasingly fee-based business model, and its reliance on the financial sector for leveraging its funds may be reconsidered. Institutional reforms could not just aim to enable the EIB to seek a more proactive policy role, but also improve the transparency of its intermediated lending operations.

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Further Information

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