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Promoting investment and growth: The role of development banks in Europe

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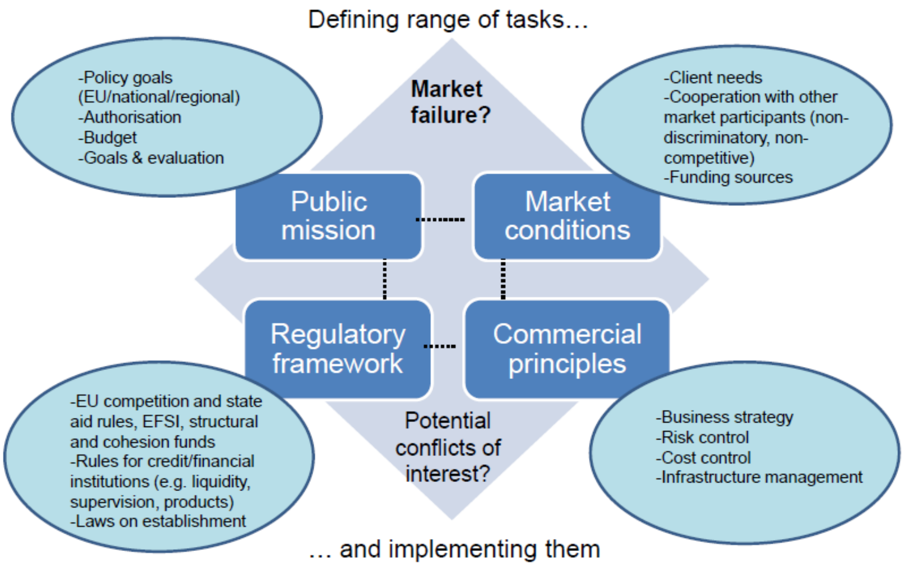
— The financial and economic crisis brought development banks back in the spotlight. They are seen as part of the economic policy toolkit for overcoming cyclical and structural difficulties in economies, complementing financial systems by improving their functioning and bolstering economic resilience. Interest in development banking to promote growth and boost investment has increased especially in Europe of late.

— Europe's promotional landscape has developed in very idiosyncratic ways resulting in a heterogeneous set of institutions operating between the state and the market. Despite their heterogeneity, they pursue quite similar goals.

— Given the current economic environment and changes in Europe's banking and financial markets, development banks are bound to continue playing an important role in the coming years. Rather than crisis relief, their focus is shifting (back) to supporting structural change in economies. Here, they can play a useful complementary role, focusing on areas of market failure.

— Risks lie with potential "overburdening" of development banks and setting expectations too high for what they can achieve. For individual entities and from a systemic perspective, the challenge will be to strike the right balance between competition and promotion.

Between the state and the market: Development banks in Europe 1



Sources: Investitionsbank Berlin, Deutsche Bank Research

Introduction

How to define a development bank? 2

Development banks are public entities, i.e. (a substantial portion of) their equity is owned by the state. Not all public banks are development banks, the latter are a subgroup. Other types of public banks are for instance postal banks and savings banks. Commercial banks can also be publicly owned. What distinguishes development banks is their mission, i.e. to promote economic development and other designated socioeconomic goals. These are typically stipulated in their mandate.

'State-owned financial institutions' is an even broader concept as it refers to financial institutions in general including – but not limited to – banks. The term includes inter alia commercial banks, development banks, leasing firms, credit guarantee funds and insurance companies that are publicly owned.

Development banks are not necessarily banks "in the legal sense", they can for instance be established and operate as special public agencies. Their legal form and organisation may depend on local requirements, their historical development, policy choices, as well as their strategies, incl. refinancing and customers targeted. Entities that get their resources from special accounts (e.g. finance ministry or central banks) are often set up as funds rather than banks (UN 2005).

While there is no fixed definition of a development bank, the Worldbank (2012) suggests that it is *"a bank or financial institution with at least 30% state-owned equity that has been given an explicit mandate to reach socioeconomic goals in a region, sector or particular market segment."* The UN (2006) defines them as "*financial institutions set up to foster economic development, often taking into account objectives of social development and regional integration, mainly by providing long-term financing to, or facilitating the financing of, projects generating positive externalities".*

Sources: De Luna-Martinez/Vicente (2012), UN (2005), Deutsche Bank Research

Since the start of the financial crisis an old concept is back in the spotlight: development banks. Credited with the ability to increase an economy's resilience by helping to cushion financing gaps in downturns as well as facilitating access to finance in areas that arguably face shortcomings, development banks are currently seen as part of the economic policy toolkit for overcoming both cyclical and structural difficulties in economies.

In the EU, grappling with the repercussions of the financial and debt crisis, debates about the role of development financial institutions (DFIs) have been particularly active lately.[1] With the financial sector undergoing restructuring and public finances often being stretched, they are seen as a way to improve access to finance, particularly for small and medium-sized enterprises, as well as helping to fund (long-term) infrastructure.

During past years, many DFIs in Europe have become more active. Several member states have reorganised DFIs or set up new institutions, others are considering doing so – all hoping to leverage their potential, promoting investment and growth. At the European level, the EIB has stepped up activity and this year the European Fund for Strategic Investments (EFSI) was established to promote investment – and ultimately growth – in Europe also via DFIs.

While DFIs have been a long-standing feature of financial and banking markets – globally, and particularly in Europe – insights into how they work and the role they play for financial markets and economic policy remain rather limited. Most research analyses DFIs in developing economies. This paper offers a different perspective and focuses on DFIs in Europe against the background of developments in recent years and the current economic policy debate.

This analysis proceeds in four steps: The first part provides a brief introduction to the concept of development banks. The second part provides a mapping of European DFIs, assessing what they do and how they operate. Part three looks at their role in addressing the financial and economic crisis. This is followed by a discussion of recent trends and their implications for DFIs, as well as for financial markets and economic policy in Europe.

Development banks in brief

Development banks are a particular type of public financial institution with a dedicated promotional mission. They are typically set up by governments to offer credit and other financial services to clients that are not served by private financial institutions to the extent desired by policymakers.[2] They are thus instruments for implementing economic policy goals.

Financial institutions to promote economic development exist and operate in practically all countries around the world. Historically, they have played an important role in fostering industrialisation, economic catch-up and to cope with periods of economic transformation. DFIs have been attracting attention recently due to their (potential) countercyclical role in economic crises and as part of a renewed discussion about the state's role in finance.

[1] Albeit to some extent in a different context, the idea of development banks, particularly to support financing for infrastructure, has recently become more popular beyond Europe, too. Take, for example, debates in the US about establishing a new infrastructure bank, China founding the Asian infrastructure and development bank or the new BRICS development bank.

[2] See De Luna-Martínez/Vicente (2012).

In addition to *national* DFIs, *multinational, regional* and *subnational* institutions to promote economic development exist. They can be linked via cooperation on programmes or joint initiatives as well as via funding.

National development institutions around the globe come in very different shapes and sizes. They differ for instance on

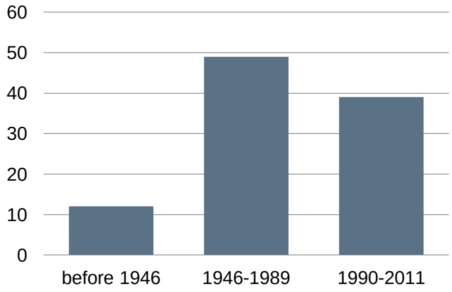
— *Ownership*: Public ownership can be full or partial. Some institutions have subnational and national owners; others a mix of national, foreign, and multilateral ownership, involving for instance other DFIs as part of development cooperation.

— *Funding,* i.e. whether they are funded via deposits, raise money on capital markets, borrow from other banks, receive budget allocations from governments or use their own equity for activities. Most institutions rely on a mix of funding sources. If debt financing is used, a key distinction is whether debt issued by development banks is (fully) guaranteed by the state.

— *Customers:* These can include individuals, firms (both private and state-owned), governments as well as other (development) financial institutions. Typically, clients include private firms. Support to SMEs is almost ubiquitous but many DFIs also target larger firms.

Development bank concept spread after WW II 3

Share of development banks established in respective period (%)



Based on global survey of development banks covering 90 institutions worldwide.

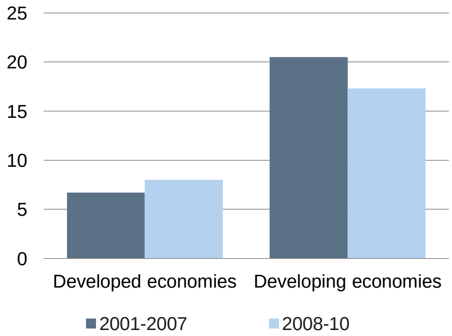
Sources: De Luna-Martínez and Vicente (2012), Deutsche Bank Research

DFIs mandates range from the general, e.g. “promoting economic development” the fulfilment of more specific tasks. For the latter, mandates define particular sectors or activities, for instance promoting agriculture or SME-financing. Globally, the distribution between “generalist” vs. “specialist” development financial institutions is about even. In a recent survey of DFIs by the Worldbank, 47% of institutions state that they operate with a broad mandate, whereas 53% have a more specific one. In terms of sectors or tasks, agriculture, SMEs and international trade are the most common areas DFIs are tasked to support globally.[3]

Some countries have several development institutions that operate at the national level, each with a dedicated sectoral or activity focus. Others have bundled different activities in one entity. What these institutions share – despite all their differences – is their public nature and a development mission.

Trends in government ownership of banks 4

Asset share of government-owned banks in the financial system (%)



Sources: Global Financial Development Report (2013), Deutsche Bank Research

Mitigating market failure is a major motivation

Theoretically, the DFI concept is linked with the concept of market failure. The reasoning here is that a functioning financial sector is vital to growth and economic development but that some financial services are underprovided in a free market setting. Establishing a DFI can be the best strategy to correct this.

Typical instances of market failure that underpin the existence of development banks and their activities are

— *Costs of information* and its *asymmetric distribution* – which may for instance underpin insufficient financing for SMEs

— *Externalities* – i.e. there are activities or projects that could be valuable to the country or community but because the benefits are difficult to appropriate, they have difficulties to attract enough funds, e.g. for climate and energy-related projects.

The market-failure argument suggests an important but complementary role for DFIs in the financial system. First of all, it provides a reason for their existence. At the same time, many controversies surrounding DFIs and their work stem from problems with defining market failure and disagreement about whether DFI intervention is the best way to mitigate it. Whether it is the best response

[3] Ibid. Based on a survey of (national) development banks.

1st vs. 2nd tier lending models 5

Direct and indirect lending models each come with pros and cons:

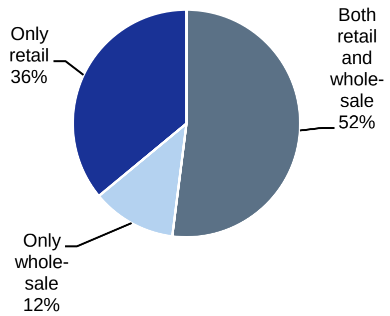
Direct (retail or 1st tier) lending models are sometimes associated with lower interest rates (no charges added by intermediaries) and DFIs can directly promote financial market development by setting up facilities in unbanked or underbanked areas. However, operating their own network increases costs for DFIs.

DFIs operating with a 2nd tier (or wholesale) model can work with a leaner structure while still reaching a lot of customers. Private institutions and DFIs can share risks. Selection and risk-assessment for loans is done by partner banks. Typically, NPL ratios tend to be lower for such wholesale models.

While the choice of lending models also reflects local market conditions, e.g. availability of commercial institutions to cooperate with as well as customer-bank relationships, 2nd tier models are often viewed as more "competition friendly" provided that DFIs work with partner banks in a non-discriminatory way.

Sources: De Luna Martinez/Vicente (2012), Deutsche Bank Research

Lending models of development banks: Mixed models dominate 6



Shares based on responses by 90 development institutions worldwide

Sources: De Luna-Martinez/Vicente (2012), Deutsche Bank Research

depends, inter alia, on the contracting environment and a government's ability to remedy market failure in alternative ways, for example via regulation, taxes or subsidies.

Views on DFIs also have been evolving in past decades from a more favourable stance (post-World War II), to a period of criticism stressing problems with political interference and inefficiencies to a more pragmatic approach that sees a valuable but limited role for them and emphasises the importance of good governance.

What they do and how they perform

What DFIs do and how they perform their role reflects both economic and political conditions. Typical activities include financing of agriculture, SMEs, international trade, housing, infrastructure and credit to local governments. Where financial markets are less developed, there is often greater emphasis on promoting general access to financial services, e.g. by offering micro-loans or acting as a deposit taker for households, and DFI activities can be very close to those of "ordinary" banks.

Development banks can lend directly to customers (1st tier/retail) or channel credit via other (private) banks (2nd tier/wholesale). Lending models again reflect local conditions to some extent: Direct lending can be the only way to reach customers in places where other financial institutions are absent or scarce. The 2nd tier model relies on cooperation with other banks who typically handle applications for loans by end customers. Globally, many development banks operate with a mix.

DFIs often provide services beyond loans and guarantees. These include venture capital, acting as business angels, leasing and factoring, securitisation as well as advisory services. Some are also active as long-term (strategic) investors.

Measuring the performance of DFIs is not an easy task because they are not meant to operate for profit, should focus on areas that are not commercially viable and play an enabling role in the economy. Hence, conventional metrics used to assess private institutions may only partly be applicable and need to be judged in reference to institutions' business models. The track-record of state-owned banks, which include DFIs, in terms of promoting general economic development, has been rather mixed. Studies have pointed out inefficiencies, potential political interference, capture by interest groups, as well as lack of clearly defined mandates.[4] To that extent, research also suggests that the institutional environment in which DFIs operate is important for their functioning and success.

DFIs in developed economies

DFIs are a common phenomenon in both developing economies as well as developed economies with relatively sophisticated and deep financial markets. In fact, some of the largest and oldest national DFIs are to be found in developed economies. They have traditionally been part of the economic policy toolkit and the financial market landscape, aiming to mitigate shortages in specific areas, such as long-term financing e.g. for infrastructure, but also providing credit to firms.

[4] For example, LaPorta et al (2002) find that a higher share of government-owned banks in the financial system tends to be associated with slower subsequent financial development and lower growth. Beck and Levine (2002) similarly do not find positive effects. See for instance Global Financial Development Report (2013) and Rudolph (2010) for an overview. On political lending see for instance Sapienza (2004) and Ianotta et al. (2011).

The financial and economic crisis triggered a “revival” of the development bank concept in developed economies. This has been driven by several factors, notably the reasoning that DFIs can play a countercyclical role, helping to mitigate the impact of economic shocks, i.e. helping to cope with the crisis and act as a stabiliser. Second, they can serve as a catalyst, promoting structural change in economies and helping to address longer-term challenges.[5] Here, the focus is more on the repercussions of the crisis, for instance addressing shortages of financing for long-term investment. Finally, in some economies, DFIs are also seen as a complement helping to improve competition on banking markets. In Europe, the potential of DFIs has attracted particular attention because of the intensity of the crisis experience combined with ongoing financial sector restructuring.

Beyond the national level: The EIB and other multilateral institutions in Europe 7

The European Investment Bank (EIB) was set up in 1958. It is owned by EU member states which hold stakes according to their respective economic weight. The bank’s primary aim is to foster European integration and balanced economic development within the union. To support this, the EIB finances and provides guidance for projects that contribute to economic growth, employment, regional cohesion and environmental sustainability. Activities focus on four pillars accordingly: i. innovation and skills, ii. access to finance for smaller businesses, iii. climate action and iv. strategic infrastructure. In addition, EIB activities support the EU´s external development policies. Most of the resources for lending are raised on international capital markets via bond issuance.

While the great majority of financing is administered via loans, the EIB also provides guarantees, equity investments and micro-finance. Since 2000 the EIB is the main shareholder of the European Investment Fund (EIF) owning 61,4% of its shares by now. The EIF is the specialist arm of the EIB focusing on providing financial resources to small and medium-size enterprises. Together with the EIB it forms the EIB Group.

In addition, there are a number of other multilateral DFIs with a particular focus on Europe, for example the European Bank for Reconstruction and Development (EBRD), or regional ones such as the Nordic investment bank or the Black Sea Trade and Development Bank operating in parts of Europe

Sources: EIB, EIF, Deutsche Bank Research

Research on DFIs, their role and functioning in developed economies remains rather limited, though. Most of the academic literature focuses on comparing public and private banks, discusses the pros and cons of state-owned financial institutions or assesses the role of DFIs in developing economies.[6] The following sections therefore provide an attempt to map the DFI landscape in Europe.

DFIs in Europe: A highly heterogeneous multi-level system

A few coordinates help to navigate: The European DFI-system has a vertical and a horizontal dimension. Vertically, there are DFIs at European[7], national and subnational level. Rather than separate layers, the different levels and entities are often linked. For instance, the German Kreditanstalt für Wiederaufbau (KfW) as a national DFI provides funding to subnational institutions in Germany. At the same time, German *Länder* own parts of KfW. Both national and subnational DFIs often play an active part in the implementation of EU policies, e.g. by helping to access EU structural or cohesion funds. The variation within the vertical dimension, for instance whether subnational institutions have been established, depends inter alia on market size, countries’ political and financial sector characteristics and their historical development.

On the horizontal dimension, i.e. comparing DFIs across member states, heterogeneity is high. Differences are less about goals or areas of activity but rather about how DFIs are organised and promotional tasks implemented. In that sense, there is a “European” DFI – the EIB – but no common model of DFIs in Europe at the member state level. Some member states have bundled different promotional activities in one national entity. Some, for instance the UK or Germany, operate several DFIs. Some do not have a dedicated DFI operating at national level (yet) – which does not mean that there are no activities to promote similar economic policy goals, such as improving access to finance for SMEs. To that extent, setting up a national DFI is just one possible way to encourage activity in selected areas. Also, it does not preclude regional institutions from emerging.

[5] See for instance the Commission’s Green paper on long-term finance in 2013 addressing the role of DFIs in financing long-term investment and growth or the discussion about the creation of an infrastructure bank in the US.
[6] There are two notable exemptions: 1. A survey by the Worldbank makes a first attempt to map DFIs globally and describe their features and functioning. The sample includes only 9 European member states though (61 in total). Schmit et. al (2011) focus on Europe but consider public financial institutions in general.
[7] This includes pan-European institutions as well as DFIs that focus on specific regions in Europe. Also see box 7.

There is no general fixed definition of DFIs in Europe or a prescription stating what they should look like. 'Development bank' to that extent remains a concept rather than a fixed category and is used to refer to public financial institutions with a specific mandate to promote economic development. While the terms "development" and "promotional" are sometimes used synonymously, European legislation typically refers to "promotional" entities.[8]

The recent communication by the European Commission on the role of national promotional banks in supporting the EU investment plan refers to national promotional banks as "*legal entities carrying out financial activities on a professional basis which are given a mandate by a Member state or a Member State's entity at central, regional or local level, to carry out development or promotional activities (..)"*.[9] Entities that fall under this header can take various forms, offer different products and operate in different ways. The reason for this is that economic policy traditions, financial markets, public sector banking – and DFIs as part of this – have developed in idiosyncratic ways across member states.[10] Entities range from specialised (supporting one sector or task) to integrated promoting multiple goals and serving several functions. Despite organisational differences, key promotional goals which DFIs pursue across Europe are quite similar, notably promoting SMEs, facilitating investment in long-term infrastructure or supporting environmentally friendly projects. These are also reflected in the vertical dimension.

What European rules provide is a framework for promotional activities and public support. This serves to preclude public support from leading to "unfair" advantages or harming the single market. Member states can set up entities which aim to advance public policy objectives and provide resources to them – but support being granted and DFIs operations have to be compatible with EU state aid rules. In this regard, the European Commission has examined the structure, financing and activities of national DFIs in the past, triggering for instance changes in the organization of German promotional banks. Also, the European Commission is assessing the creation of new DFIs with respect to compatibility with state aid rules.[11]

Public financial institutions between state and market

DFIs can be conceptualised as a special type of entity which forms part of the public financial sector.[12] Theoretically, a distinction can be made between various types of public financial entity (see box 8). However, these are ideal types and in practice, the boundaries between them are more blurred. A DFI may also be active as a long-term investor or offer programmes to support companies' exporting activities. Take for instance Finland's Finnvera group or Romania's EXIM bank, where one part of the group aims at promoting SMEs whereas another operates as an export credit agency.[13] Other member states have chosen to establish a separate entity for the latter task. Similarly, many DFIs offer credit to municipalities. This can be done as part of the operations of a national DFI, in a separate (national) entity and/or by regional DFIs.

Locating DFIs in the European (public) financial sector landscape — 8

DFIs are a particular type of financial institution forming part of the public financial sector and benefiting from support for their activities. Public financial entities can be classified in different types:

1. Public savings banks
2. Public financial intermediaries, e.g. Landesbanken (DE)
3. Long-term investors, e.g. Caisse des depots et consignations (FR)
4. Special Credit institutions
   i. Municipal credit institutions, e.g. Kommunekredit (SE), Bank Nederlandse Gemeenten (NL)
   ii. Export Credit agencies, e.g. Export Credit Guarantee Company (MT), SACE (IT)
   iii. National and subnational DFIs

Sources: Schmit et. al. (2011), Deutsche Bank Research

Consolidation or functional differentiation? — 9

Public financial institutions are a typical feature of European countries' banking and financial systems. They have traditionally played a role in supporting economic policies and providing financial services to the public sector.

EU member states differ with respect to how these activities are organised and to what extent a dedicated national DFI performs them. In terms of regional patterns, DE, IT, ES or CEE tend to have more integrated national DFIs which perform several tasks such as promoting investment in infrastructure, providing financing to regional authorities etc. ("consolidated model").

In contrast, Scandinavian countries and the Netherlands tend to have municipal credit institutions which provide financial services to public entities and for instance help to finance public infrastructure development with a dedicated local focus. In addition, there are "issue-specific" institutions, for instance to promote SMEs, financial institutions with a specific sector focus (agriculture, housing) and joint regional initiatives (e.g. the Nordic Investment Bank) to promote investment in infrastructure ("differentiated model").

Source: Deutsche Bank Research

[8] Different pieces of legislation contain definitions of "promotional lenders" though to provide guidance at the operational level, e.g. with regard to related supervisory reporting obligations. See for instance Delegated Act to supplement Regulation (EU) 575/2013 with regard to liquidity coverage requirement for Credit Institutions Art.10 defining a subset of credit institutions as promotional lenders.
[9] See p.3 COM 2015(361/2). Also see EFSI regulation Art.2 for a similar definition.
[10] For an overview of public banking in Europe see Schmit et al (2011).
[11] See for instance the recent cases on UK's Green Investment bank, British Business Bank, the Portugese Instituição Financeira do Desenvolvimento and the new Latvian DFI.
[12] See Schmit et. al. (2011).
[13] European competition law requires that competitive activity is organised in a separate entity. The promotional business must be not for profit.

On balance, this leaves the promotional landscape in Europe fragmented and idiosyncratic and results in a heterogeneous set of entities pursuing economic policy and development goals.

In theory, a DFI in Europe could be defined by three criteria, i.e.

i. A dedicated development mandate set out in law
ii. Public ownership
iii. Competitive neutrality.

In terms of analysing national DFIs empirically, this implies several challenges:

— Mandates are defined at national (or subnational) level

— Organisational forms can be different reflecting local laws and market conditions and hence information about DFIs is anything but standardised

— Delineating DFIs from other types of public financial institutions

— Delineating commercial and development activities

— Considering individual institutions as part of their operating context, including how they interact with the rest of the financial system, what close substitutes to DFIs may have developed etc. as this also affects what individual institutions look like and which tasks they perform.[14]

Nevertheless, the following analysis attempts to provide some cross-country comparisons to identify main characteristics. Rather than a list, this should be treated as an indicative mapping – all the more because the DFI landscape in Europe has been undergoing changes recently.

The analysis focuses on identifying the main institutions to promote economic development operating at national level. While two sectoral DFIs are included (UK Green investment bank and German Landwirtschaftliche Rentenbank) the main emphasis is on entities to support SMEs and investment in (long-term) infrastructure, which have traditionally been important areas. For a majority of cases, the main DFI(s) can be clearly identified. In total, 24 entities located in 22 EU member states are considered. In addition, the appendix provides an overview and additional information on promotional activities for each member state. For some countries which have only recently set up a dedicated national DFI or restructured existing ones, data availability is limited.

List of DFIs considered — 10

1. BE: -*
2. BG: Bulgarian Development Bank
3. CZ: Czech Moravian Guarantee and Development Bank
4. DK: -*
5. DE: Kreditanstalt für Wiederaufbau and Landwirtschaftliche Rentenbank
6. EE: KredEx
7. IE: *Strategic Banking Corporation*
8. GR: *Institute for Growth*
9. ES: Instituto de Crédito Oficial
10. FR: *Banque Publique d'Investissement*
11. HR: Croatian Bank for Reconstruction and Development
12. IT: Cassa Depositi e Prestiti
13. CY: -*
14. LV: *Altum*
15. LT: Invega
16. LU: National Credit and Investment Institution
17. HU: Magyar Fejlesztési Bank Zártkörűen Működő – Hungarian Development Bank
18. MT: -*
19. NL: -*
20. AT: Austria Wirtschaftsservice (aws)
21. PL: BGK Bank
22. PT: *Instituição Financeira do Desenvolvimento*
23. RO: EXIM Bank
24. SI: Slovenska izvozna in razvojna banka
25. SK: Slovenská záručná a rozvojová banka
26. FI: Finnvera
27. SE: Almi
28. UK: *British Business Bank and Green Development Bank*

* For countries listed with " - " also see the appendix for further information. *Italics* refer to entities that have been set up or reorganised since 2012.

Source: Deutsche Bank Research

Establishment

Four main foundational periods of DFI formation in Europe can be distinguished:

1. Pre-1945

Historically, some European DFIs trace their roots back to the 19th century when they played an important role fostering industrialisation. This is the case in France or Italy, where some of the oldest institutions still existing were established. Caisse des dépots et consignations, involved in today's French DFI, BPI, as an owner, was set up as early as 1816 after the collapse of the Napoleonic empire. Italian Cassa depositi e prestiti was founded in 1850. In the absence of modern retail banking structures, they also played a role as a safe place to put deposits. Funds were then used to finance for instance public infrastructure projects. Early DFIs also included sectoral development banks; e.g. Landwirtschaftliche Rentenbank (DE) traces back its roots to the 1920s

[14] Arguably, there is a difference between analysing promotional activities and how they are organised and comparing development financial institutions as such. At the same time, comparing institutions without considering their operating context could easily lead to incorrect conclusions for instance when comparing the size of entities or their role in financing of a specific sector.

when the predecessors of the current institution were established.[15] In terms of geographic scope, DFI formation was not limited to Western Europe with DFIs for instance being set up in Poland in the 1920s as well.

2. 1945-1989

Two of Europe's largest DFIs were established during this period, i.e. KfW (DE) and ICO (ES) albeit under different circumstances. KfW was set up in 1948 to support rebuilding the economy after WWII. Austria's Bürgesbank (1954), is a similar case, with promotional activities also benefiting from US recovery aid. Spain's ICO was set up in 1971 to coordinate and control the country's state-owned banks.

3. Post 1989

CEE countries saw a wave of DFIs being established in the early 90s, incl. institutions in SK, SI, RO, CZ and HR. Institutions were set up with a focus on promoting economic transformation in transition economies.

4. Since 2008

Currently, there is a new "foundational phase" going on with PT, GB and IE having set up new institutions, some member states reorganising existing ones (FR, LV), and a number of countries considering changes and/or the establishment of new DFIs (including MT and GR, for example). The main focus is on tackling the impact of the crisis in the respective economies, with both long-term and SME financing being key areas of DFIs to address.

Not all EU member states currently operate dedicated national DFIs with an SME or long-term investment focus. Having said that, this does not imply that there are no promotional activities in these areas – funds can for instance be channelled via commercial banks or regional institutions play an important role. Belgium for example has transferred promotional tasks for SMEs to regional funds recently, discontinuing the national fund, and has a tradition of channelling funds via commercial banks.

The brief look into DFI history shows that they have often been set up as a response to crises and structural economic challenges. Helping to mitigate budgetary shortages and improving access to finance for firms have been key motivations from the start – and continue to be at present.

The form and activities of DFIs have reflected the structure and specific needs of member states' economies, financial markets, and policy priorities. Hence, heterogeneity has always been high. DFIs have also kept evolving over time, mirroring changes in political and economic circumstances.

Arguably, the two most recent foundational periods were somewhat less divergent, because knowledge transfer and learning among DFIs has played a greater role. Also, DFIs have already been established within a "European framework" from the start – particularly those founded since 2008 –rather than adapting existing entities to fit with common rules.

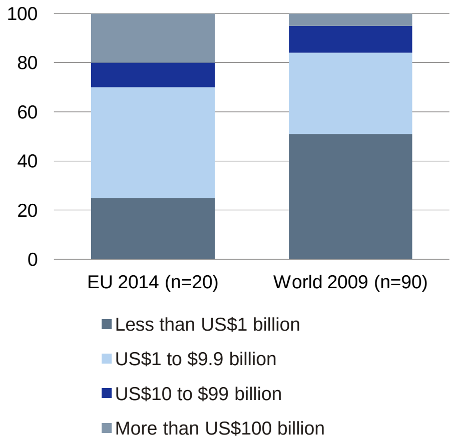
Most of the recently established institutions emphasise improving access to finance for SMEs. Britain's Green Investment Bank is the exception as it has a dedicated focus on promoting investment in "green infrastructure and technologies". Many established DFIs support "green" projects as part of their normal business, though.

[15] This concerns Deutsche Rentenbank and Deutsche Rentenbank Kreditanstalt. Landwirtschaftliche Rentenbank as their successor which still operates today was established in 1949. See https://www.rentenbank.de/dokumente/Historie.pdf and Gothe (2014) for further information.

Size of DFIs

Composition of DFI group by total assets 11

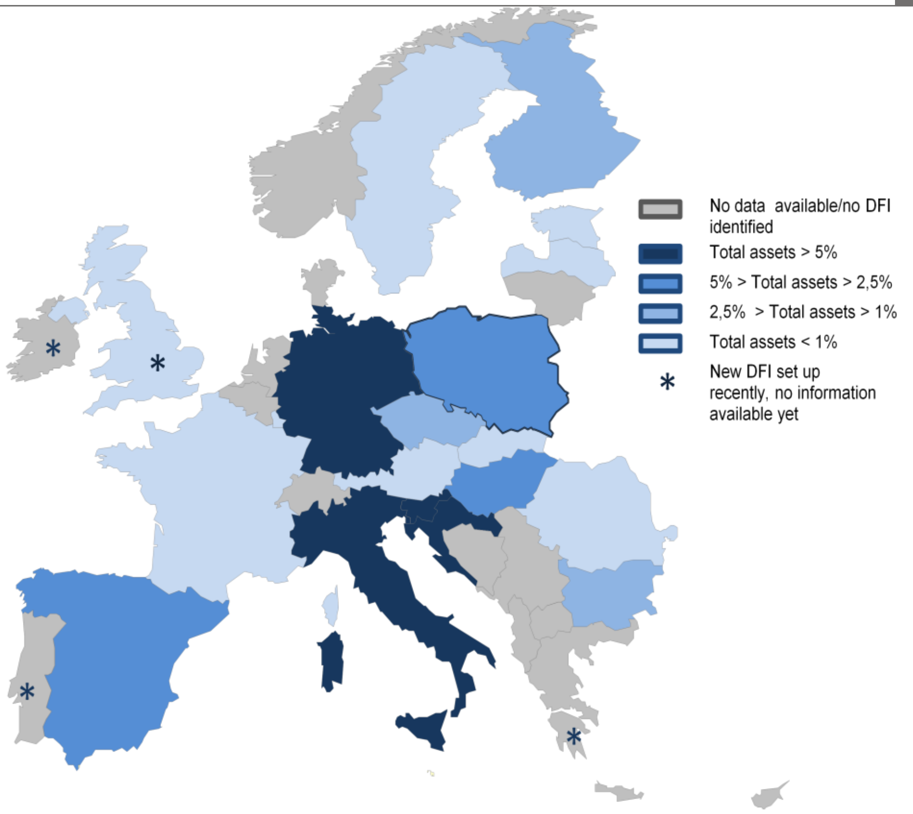
Percentage share of institutions for the respective categories



Sources: De Luna-Martinez/Vicente, Deutsche Bank Research

In terms of total assets[16], few European DFIs would be considered small by global standards. Following the World Bank's categorisation, two European DFIs would count as large and four as "megabanks".[17] By far the largest DFI is KfW. Notably, even some of the subnational promotional entities in Germany would qualify as (very) "large", according to this categorisation.[18] The smallest institutions are located in the Baltics (LV, EE). By balance sheet size, institutions in new member states tend to be smaller than entities which have existed for some time already in old member states.[19] Measured relative to the size of national banking systems though, this is less clear-cut and some of the relatively larger DFIs are located in CEE countries.

European DFIs relative to national banking systems 12



Sources: ECB, company reports, Deutsche Bank Research

Relative to their national banking systems, European DFIs are actually not that large compared to global peers. Some DFIs in developing or emerging economies have shares exceeding 10% in their respective markets.[20]

Limits of simple size comparison

While informative, DFI size comparisons need to be treated with caution. First, size gives limited information on a DFI's significance to the economy. They can be small and still play an important role, having a large share in specific markets

[16] Based on total assets as listed in annual reports. It should be noted that institutions operate with different business models and organisational structures. Level of consolidation and accounting rules used can impact on measurement of total size.
[17] This is based on 20 entities, i.e. not considering new DFIs in IE, PT and GR and only Green Investment Bank for the UK.
[18] For example NRW-Bank (total assets of EUR 143 bn in 2014) or L-Bank (EUR 70 bn).
[19] Considering median values by group.
[20] See De Luna-Martinez/Vicente (2012).

or improving their functioning. Some activities they engage in may have a limited impact on their balance sheet size, e.g. seed and start-up funding or advisory services, but are still of relevance to the economy.

Second, with regard to individual entities, size also depends on how promotional activities are organised, i.e. whether they are specialised DFIs or entities performing multiple tasks. The financing arm of French BPI for instance is relatively small when comparing its size with KfW or CdP. However, this would neglect BPIs group structure and that it plays a different role in the French banking system because alongside BPI, Caisse des dépots et consignations has traditionally been important for channelling funds from savings into infrastructure and housing finance. Hence, individual entities' position as part of the public financial sector and the financial system at large also play a role.

Finally, there is a difference between comparing DFIs as (group) entities and promotional activities benefiting from public support, because institutions often operate different activities within one group. This is for instance the case with KfW where KfW Ipex operates as a separate subsidiary within the group and conducts commercial business, or the new British Business Bank which also has a commercial arm alongside its mandated business.

Size therefore remains a limited proxy for capturing a DFI's role for the respective economies or comparing DFIs across countries.

Ownership and organisation

Full public ownership is the prevalent model among European DFIs. In this respect European DFIs are similar to their global peers (see box 13). In some cases (DE, RO), public ownership is split between the federal and state level, i.e. subnational entities also take stakes in national DFIs. Italy's CdP is an exception with regards to ownership structure – while the Ministry of Economy and Finance is the major shareholder (80.1%), 18.4% is held by banking foundations. Italian banking foundations, though, have their roots in public sector banking and are not meant to be for profit. Similarly, France's Caisse des dépots, itself a public group, takes ownership stakes in BPI.

Altogether, a DFI's ownership structure as well as its legal form are largely a reflection of its founding history and evolution rather than regional patterns. In Germany, for instance, there is also variation among the two national and 17 regional promotional institutions: some are wholly state-owned (federal or state level), in others savings banks participate and one entity also has private banks as minor shareholders.[21] Similarly, there is a variety of legal forms, with German DFIs including one public limited company and several corporations under public law (Anstalten des öffentlichen Rechts), operating independently or public law corporations operating within Landesbanks (Anstalt in der Anstalt).

All in all, ownership and organization of DFIs in Europe shows their integration with the public (financial) sector and their special role operating between the state and the market. Public ownership is reflected in governance structures, with governments providing strategic direction. DFIs' special status also implies an incentive for public-sector owners to provide support if need be. Also, many are not subject to ordinary corporate bankruptcy law.[22]

DFI ownership and funding worldwide 13

Globally, about three-quarters of DFIs are wholly owned by governments which also provide strategic direction and are often involved in the selection of board members. About 20% of institutions worldwide are majority state-owned (50-99%). DFIs with state-ownership lower than 50% are the exception.

In terms of funding, DFIs around the world typically rely on a mix of sources. Most DFIs can borrow from other institutions or issue debt in local markets (provided government approval). For about two-thirds, debt is guaranteed by government.

About 40% receive direct budget transfers. This does not imply dependence on government funding, though, because it can constitute an only small share or transfers may be used to fund interest rate subsidies for particular programmes or types of borrowers.

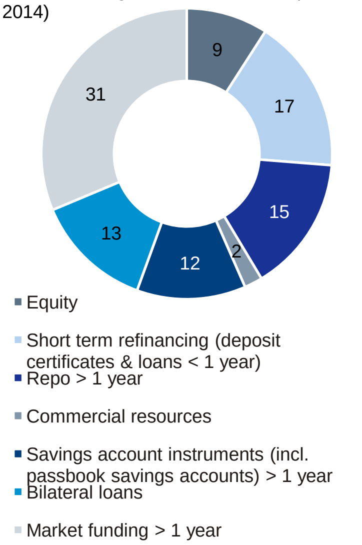
About 41% take deposits from the general public. Deposit funding is often viewed sceptically because it implies that DFI operations are closer to commercial banking, potentially raising competition issues. Deposit taking institutions tend to lend directly to customers, too.

Sources: De Luna Martinez/Vicente (2012), Deutsche Bank Research.

[21] See VOEB (2013) for an overview. In the case of Landwirtschaftliche Rentenbank the principal was raised through a special levy on the agriculture and forestry sector. The Federal Republic of Germany guarantees liabilities and the bank's existence through Anstaltslast.
[22] See Fitch (2015). This does not preclude the possibility of entities being reorganised or that their status may change over time.

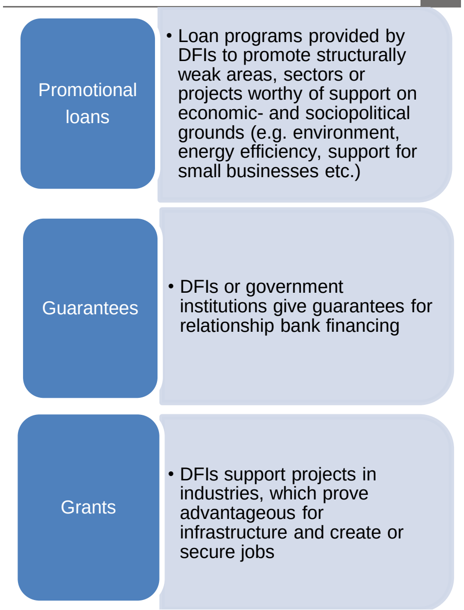
Diversified refinancing - a European example 14

Bpifrance refinancing structure, shares in percent (Dec. 2014)



Sources: Bpifrance, Deutsche Bank Research

Promotional instruments 15



Promotional loans and guarantees can also be provided as global loans: DFIs contract with cooperating banks, providing them with a lump sum of funds which are then passed on by banks to customers according to specified criteria.

DFIs can also act as investor, i.e. taking equity stakes in companies, or play an enabling role, e.g. by providing information and advice.

Source: Deutsche Bank Research

Funding

Similar to global peers, European DFIs have a mixed funding base. Most European DFIs are not allowed to directly take retail deposits for funding, reflecting their special status (they may take deposits from other banks, though). Bulgaria's BDB is an exception and Italy's CdP indirectly relies on deposit funding via postal bonds and passbook accounts.

Most institutions source parts of their funding on capital markets by issuing bonds – and some are quite important issuers. Ratings for DFIs mirror those of the sovereigns providing guarantees due to expectations of timely support. While there are guarantees for debt in most cases, this is not always the case (e.g. BG) or there are limits to guarantees (e.g. IE).

A number of entities also get some funding from other DFIs, particularly the EIB and other European DFIs but occasionally also including DFIs based outside Europe. Funding from European programmes that are distributed via DFIs plays an important role for some DFIs (e.g. HU, BG). In general, DFIs in weaker economies tend to be more reliant on EU and owners' funds for their operation.

Funding also reflects organisation to some extent, i.e. different business arms can have different funding strategies. Sometimes there are restrictions in terms of the use of funds, either because funding relates to support for a specific program and/or parts of an institution may not tap a particular funding source due to its different operations and risk profile.[23]

Business models, operations and products: Recent trends

European DFIs have adopted different business models to conduct their lending operations. Most institutions cooperate with the commercial banking sector, i.e. they channel promotional funds through other financial institutions that then lend-on to end-customers. Second-tier lending tends to be particularly dominant in countries where relationship banking is strong (e.g. DE and ES). Some other institutions, e.g. Bulgaria's BDB, place greater emphasis on direct lending; a small number particularly in CEE still operate a domestic branch network and show greater proximity to commercial banking.

With regard to organisation, some member states (FR, UK, LV) have recently been reorganising promotional activities, bundling similar activities in one organisation to facilitate access and increase efficiency.

In terms of products, EU DFIs typically offer guarantees and loans as well as a number of additional services beyond and around these "traditional" products, including for instance advisory services and training. Many DFIs have set up instruments to particularly support young firms such as seed funds or venture capital. Some also take equity stakes in companies acting as "strategic investors" (IT, FR, LU).

In addition, participation in EU programmes and making funds accessible is a major part of the business for many European DFIs – particularly in structurally weaker regions.

Despite the heterogeneity of institutions and different local market conditions one issue that most DFIs currently seek to address is promoting internationalisation of small and medium-sized firms with a view to improving their competitiveness and potential for export.

[23] BPI for instance distinguishes between its participation and financing arm.

European DFIs operating between the state and the market

DFIs operate between the state and the market in Europe. They play a policy role and governments provide their strategic priorities. While they are financial market participants, they often have a special status in financial systems. This is also reflected in their governance and supervisory structures.

Again, heterogeneity is pronounced. Some entities are very similar to ordinary banks to the extent that they operate with a banking license and are covered by banking supervision. For most though special rules apply. Supervision and governance structures reflect their hybrid role between the state and the market.

The following section compares four DFIs from DE, IT, ES and FR across different dimensions.

Four DFIs in comparison 16

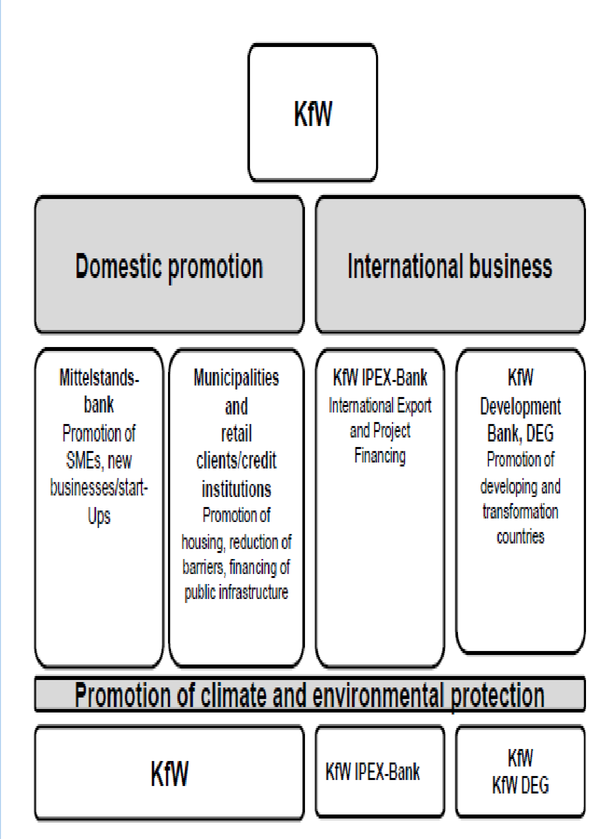
Kreditanstalt für Wiederaufbau - KfW

Established: 1948
Owner: 80% Federal Republic of Germany, 20% German states

KfW is Germany's main DFI at national level. It supports financing of infrastructure, SMEs, housing and environmental projects mainly in Germany. KfW is also active in export and project financing as part of its international business and development cooperation. It also takes on special tasks (e.g. privatisation).
Its main business areas are:
i) Mittelstandsbank (small business banking)
ii) Kommunal- und Privatkundenbank (municipal and retail clients/credit institutions)
iii) Export and project finance
KfW holds several participations, incl. wholly owned subsidiaries (KfW IPEX and DEG) as well as some German companies, e.g. infrastructure providers.

KfW has played an important role in financing reconstruction of the German economy following WWII. It has traditionally operated with quite a wide mandate and continues to support German economic policy via promotional activities. Funds are mostly channelled through commercial banks. KfW was also active in implementing Germany's fiscal stimulus package 2009/10 and assumed EUR 15.2 billion of Germany's contribution to the loan package from euro-area member states to Greece (government-guaranteed).
Total assets: EUR 489 bn (2014)
Consolidated profits: EUR 1,514 m (2014)
Legal form: Anstalt des öffentlichen Rechts (public law institution). KfW Ipex operates as an independent subsidiary conducting commercial activities
Refinancing: Mainly wholesale
Public support: Statutory guarantee covering all liabilities and maintainance obligation as guarantee for KfW as an economic entity (Anstaltslast & Gewährträgerhaftung). KfW IPEX does not benefit from an explicit government guarantee
Supervision: As a public law institution, KfW is subject to its own governing laws and statutes. It does not have a banking licence. An amendment to KfW law permits the Federal Ministry of Finance (together with the Federal Ministry for Economic Affairs and Energy) to declare provisions of European and German banking regulation applicable to KfW. The Federal Financial Supervisory Authority (BaFin) has taken on supervision of such provision but KfW's legal supervision is with the Ministries of Finance and Economics.
Governance: the Ministers of Finance and Economics preside over the supervisory board (Verwaltungsrat), alternating each year. Supervisory board with 37 members includes several ministers, members of parliament as well as private sector and trade union representatives
The Mittelstandsrat – chaired by the Minister of Economics – specifies the mandated tasks of Mittelstandsbank, consults and decides on support

Organisational structure



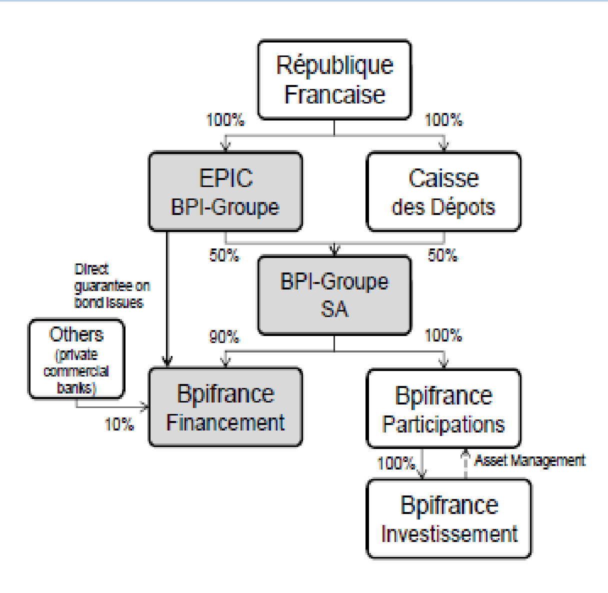
Banque Publique d'investissement - BPI

Established: 2012 (Bpifrance 2013)
Owner: 50% French state (via EPIC-BPI Groupe)
50% Caisse des dépots et consignations (itself government-owned)

BPI is a public group to support financing and development of companies, supporting public policies by the State and the Regions. BPI consolidates the activities of several entities that previously acted separately. OSEO (to support SMEs) now operates as BPI financement. In addition, BPI has an investment and a participation arm.
BPI's main aim is to support growth, employment and competitiveness of the French economy and its prime responsibility is to safeguard the state's economic interest. To further this aim, it provides loans and equity financing, supporting industrial policy and strategic sectors.
Total assets: EUR 59.7 bn (2014, Bpifrance consolidated)
Consolidated profits: EUR 130 mn (Bpifrance, net income)
Legal form: établissement public à caractère industriel et commercial (public company)
BPI Groupe is classified as a central government body
Refinancing: BPI Groupe benefits from an implicit guarantee from the State
BPIfrance Financement as a subsidiary benefits from an explicit guarantee by EPIC BPI-Groupe
Supervision: BPI-Groupe is under the supervision of both the Ministry for the Economy, Industry and Employment, and the Ministry for Higher Education and Research. The six members of the EPIC Board are appointed by the State.

Bpifrance Financement and BPI-Groupe SA are under the permanent control of a Government Commissioner (with the power to veto some of the Board of Directors' decisions) and supervised by the French Banking Authority (ACPR), the ECB and the Financial Markets Authority (AMF)
BPIfrance is under common supervision and supervised directly by the ECB (BPIfrance Financement and BPIfrance Régions).
Governance: The CEO is appointed by decision of the Minister for Finance and Public Accounts and the Minister for the Economy.

Organisation and ownership structure



continued

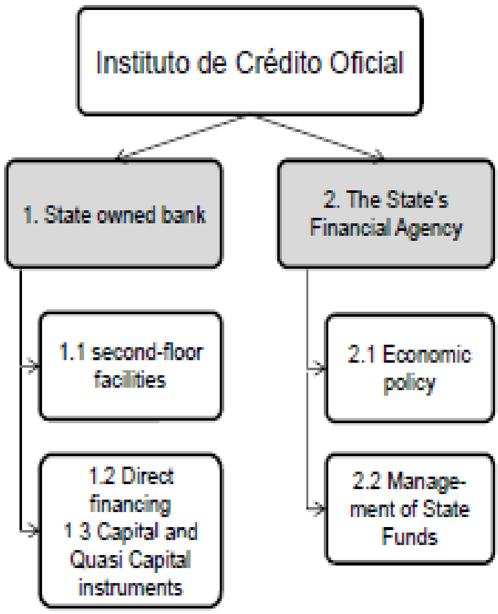
Instituto de Credito Oficial – ICO

Established: 1971
Owner: 100% Kingdom of Spain

ICO's purpose is to support and foster economic activities which contribute to the growth and improved distribution of national wealth. ICO is the state's financing agency and a state-owned promotional bank. It was created in 1971 as the institution responsible for co-ordinating the state-owned banks existing at the time.
Main activities are support to SMEs via loans channelled through other banks ("second-floor facilities"), long-term loans in sectors of national interest, managing export-promoting financial instruments. ICO also supports initiatives to develop less wealthy regions in Spain and can provide support, e.g. in case of natural disasters and economic crisis. In addition, it operates concessionary lending programs for developing countries.

ICO group also comprises a venture capital firm (Axis) and the fundación ICO. ICO also participates as a shareholder in other entities, e.g. the Spanish development corporation (COFIDES).
Total assets: EUR 84 bn (2014)
Consolidated profits: EUR 74 mn (2014, net income)
Legal form: Bank + Special status as Spain's government financial agency
Refinancing: mainly interbank and wholesale bond issuance, bonds benefit from state guarantees. Also some financing from other development institutions (incl. KfW, EIB).
Public support: State guarantees on all debt and possibility of capital injections
Supervision: ICO is a credit institution from a legal point of view and is treated as a State Finance Agency with its own legal status to carry out its activities. Not under common supervision by the ECB but supervised by national authorities and following rules and regulations as private banks.
Governance: ICO is governed by a General Board. It comprises the Chairperson of ICO, who also chairs the Board, and ten members. The Spanish cabinet is responsible for appointing and dismissing General Board members, at the proposal of the Ministry of Economy and Competitiveness. Members are selected based on their professional renown and competence in the scope of ICO's activities. Four of the ten members of the General Board are independents (not public servants).

Organisation and function

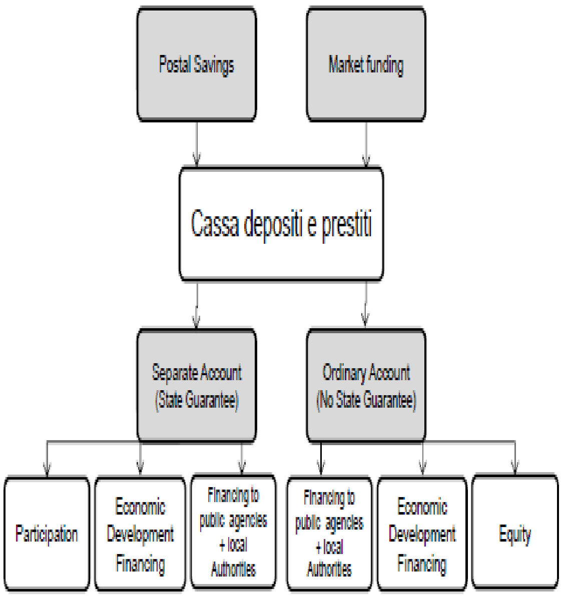


Cassa depositi e prestiti - CdP

Established: 1850
Owner: 80.1% Italian Ministry of Economy and Finance
18.4% various bank foundations
1.5% treasury shares

CdP aims to foster the development of public investment, local utility infrastructure works, and major public works of national interest.
Traditionally publicly mandated lending activity, loans to state, regional and local governments and public law entities for financing of capital investments.
CdP widened its scope of operations in recent years to include for example SME financing, additional support for exporters (with SACE) and projects carried out via PPP. CdP can also participate in investment funds and acquire equity holdings in companies of strategic interest. For instance, it holds controlling stakes in utilities of national importance.
Total assets: EUR 350 bn (2014)
Consolidated profits: EUR 2,660 m (2014)
Legal form: Sozietà per Azioni
Refinancing: Main sources are postal savings products (passbook accounts & postal bonds)
CdP also issues bonds to retail investors. Beyond retail funding CdP also obtains funding from institutional investors and, for example, launched new programmes for medium- and short-term funding in 2014/15.
Public support: CdP's main source of funding, i.e. postal savings, is government guaranteed. For other funding state guarantees are possible but several bond programmes are not state-guaranteed.
There is organisational and accounting separation for different activities of CdP (ordinary account, special account and joint account operations).
Supervision: CdP has a special status, not regulated by Italian banking law but has adopted bank accounting standards. Subject to national supervision (Italian Central Bank) under a special prudential regime. It has to comply with minimum reserve and statistical reporting requirements but not minimal capital requirements.
CdP remains subject to parliamentary control and public sector audit by Corte dei Conti
Governance: The Board of Directors has nine members. For the administration of the Separate Account, which pursues objectives of general economic interest, the Board is supplemented with representatives of the Ministry for the Economy and Finance and local government. Also, there is a parliamentary supervisory committee to control CdP, made up of members of parliament (representatives of the Chamber of Deputies and the Senate) and non-parliamentary members (representatives of the Council of State and the State Audit Court).

Organisation and funding structure



While each of the entities has its own history and structure, there are some similarities. Both KfW and ICO have developed as "integrated" DFIs, providing lending services to both public-sector clients and companies. They also have a tradition of channelling promotional funds through other commercial banks, which reflects reliance on relationship banking ("Hausbankprinzip").
CdP has a tradition in providing loans to public authorities and only recently broadened its scope to SME financing, venture capital etc. Similarly, BPI was only recently set up as an integrated entity to pursue both SME promotion and investment activities, whereas Caisse des dépots et consignations has traditionally played a role as a long-term investor. France and Italy are also similar to the extent that they have a tradition of "channelling" retail savings via guaranteed products into public DFI operations and infrastructure investment.
In each of the four cases, the set-up, structure and development of the DFI ultimately reflects a mix of history, economic policy traditions, financial market structure and public participation.

Sources: Company websites and presentations, Fitch, Deutsche Bank Research

Bank ownership and cyclical lending patterns 17

— Micco and Panizza (2006) find that lending by state-owned banks tends to be less procyclical compared to private banks for a global sample of 6,628 banks between 1995-2002.

— Ianotta, Nocera and Seroni (2011) consider 210 western European banks between 2000 and 2009. They find no significant difference in lending behaviour between public and private banks.

— Cull and Martinez-Pereia (2012) focus on Latin America and Eastern Europe from 1999 to 2009. Their results suggest that ownership matters – but effects are contradictory for different regions: state-owned banks acted countercyclically in Latin America but not in Eastern Europe.

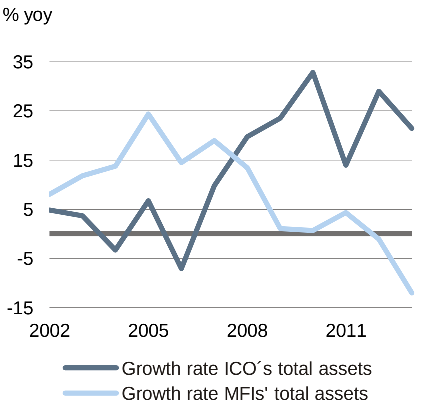
— Calderon (2012) examines to what extent the shape of credit cycles differ, depending on public bank presence. Analysing a dataset that covers 66 countries from 1980 to 2010, he finds that credit cycles are deeper in countries with a high share of state-owned banks, while recoveries from a contraction in credit are faster.

— Bertray et. al (2012) examine a global sample of 1,633 banks covering the time span from 1999 to 2010. Their findings suggest that in countries with “good governance”, state-owned banks operate less procyclically than private banks and even countercyclically in high-income countries.

While most recent research suggests some support for DFIs’ countercyclical role, the empirical literature on bank ownership and lending cycles typically does not distinguish between different types of public institutions, i.e. it considers government-owned banks in general rather than DFIs specifically. Also the focus on lending does not capture other DFI activities to provide support.

Source: Deutsche Bank Research.

Bank assets in Spain: ICO against the trend 18



Sources: ECB, Deutsche Bank Research

European DFIs in the crisis

In the wake of the financial and debt crisis, three main trends for DFIs in Europe can be observed: 1. Extension of activities in terms of scale, 2. Extension of activities in terms of scope, 3. Europeanisation.

The global financial crisis reignited the debate about DFIs’ potential to play a countercyclical role, thus mitigating recessions.[24] While empirical studies on countercyclical lending have tended to show mixed results, more recent analyses suggest that it has had a balancing effect, particularly in high-income countries during the early years of the financial crisis.[25] While panel studies often consider public banks or SOEs in general, increased activity is also observable when looking at European DFIs individually, considering develop-ments in the most recent years against the background of the European debt crisis.

Examples of countercyclical activity include

— Spain’s ICO more than doubled loans between 2007 and 2013; inter alia it granted EUR 5.3 bn of ad-hoc credit to autonomous communities in H1 2012 to help them refinance debt maturities[26]

— Italy’s CdP increased loans to banks and customers by EUR 11 bn (+12%, 2010-2014)[27]

— Loans to banks and customers more than doubled from 2008-2013 at SID (SI) and increased by about 30% at Bulgarian Development Bank (2007-2013)

— Germany’s KfW launched a special programme in 2009/2010 to support SMEs, issuing EUR 13.3 bn of credit[28]

DFIs not only increased lending, they also extended their scope and took on additional activities.

— Lithuania’s Invega provided temporary assistance to large enterprises by providing guarantees with a total budget of up to LTL 150 m in 2009/2010[29].

— SID provided temporary guarantee schemes for corporates and individuals in 2009 on behalf and for the account of the state as part of stimulus measures[30].

— Finnvera extended its business beyond SME support by also lending to larger companies and the institution’s capacity for risk-taking was increased.

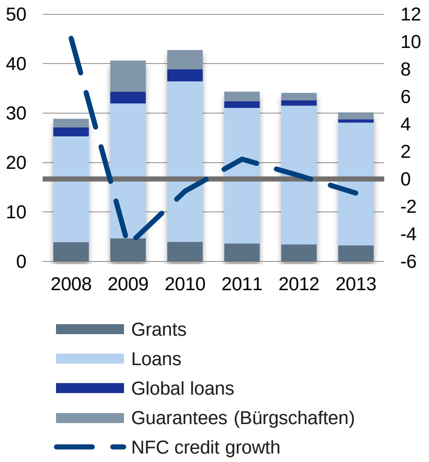
— ICO contributed EUR 6.3 bn to a special purpose fund to pay off arrears of local governments. Spain set up a mechanism to support the liquidity of local and regional governments in 2012. ICO plays a key role as a payment agent of the facility that was set up to cover regions’ maturing debt and authorized deficits.

— Austria’s aws played an active role in administering the economic stimulus package in 2009/2010.

[24] See for example Rudolph and IMF (2013) for discussion.
[25] See for example Bertray et. al (2012).
[26] See Fitch (2013).
[27] See http://www.cdp.it/annual-report/en/2014/grafici-interattivi.html
[28] See KfW annual report 2010 https://www.kfw.de/Download-Center/Finanzpublikationen/PDF-Dokumente-Berichte-etc./2_Jahresberichte/KfW-Jahresbericht-2010-DE.pdf
[29] Communication from the Commission – Temporary Community Framework for state aid measures to support access to finance in the current financial and economic crisis by the Government of the Republic of Lithuania.
[30] See SID bank’s annual report 2014, p.16.

Countercyclical patterns in Germany 19

Left: Promotional activity targeting corporates ("gewerbliche Förderung") by special credit institutions in DE, (EUR bn)
Right: Total NFC credit growth, (% yoy)



Sources: VOEB, ECB, Deutsche Bank Research

Cyclical market failure 20

Economic literature points to two cases of "cyclical market failure" that can justify intervention:

1. Coordination failure argument (Levy et al. 2004): Private banks have limited appetite to lend during periods of economic downturns and low interest rates. Increasing lending (to push the economy out of recession) would be beneficial, but this effect is not internalised by private banks. More lending by DFIs can be useful in this case as it helps to solve the coordination problem and to eventually escape the recession.

2. Risk-spreading argument (Arrow and Lind 1970): Banks' risk aversion can be procyclical and amplify economic cycles. If banks become more risk averse in an economic downturn consequentially reducing lending, this can further intensify a recession. Government actors have greater risk-bearing capacity (diversification, patience), thus helping to absorb the reduction of loans by banks and smooth the economic cycle.

Sources: Gutierrez et. al (2011), Rudolph (2010), Deutsche Bank Research

In addition, past years also saw further Europeanisation in a number of ways. This related to activities by national DFIs as well as the increased role of the EIB in crisis management.

— National DFIs have supported each other. This was done via several channels including the provision of credit as well as DFIs providing advice to peers or to governments planning to set up new institutions to promote economic development. For instance KfW provided global loans (Globaldarlehen) to CdP, ICO, and – together with France's BPI and the EIB – financing and advice to set up the new strategic banking corporation in Ireland.

— Notably, the EIB increased lending following a EUR 10 bn capital increase in 2012 that enabled additional financing of projects in the range of EUR 180 bn between 2013 and 2015. EIB also contributed EUR 5 bn to the EU's new EFSI (European Fund for Strategic Investments)[31] from own resources. At the same time, several member states have contributed to EFSI via their national promotional banks. Also, national DFIs cooperate with the EIB on EFSI projects.

Providing advice and cooperation between development banks is nothing new in principle. Similar arrangements have already existed for CEE countries for a number of years. What is different this time is i) the creation of a joint facility to promote investment in which national DFIs can take part and ii) that the discussion about DFIs role and their potential for European economies is not only regionally focused. Rather, DFIs are considered as part of the economic policy toolkit to address problems on a national as well as on a European scale.

From a theoretical perspective, stepping up DFI activity can be useful to balance private banks' greater reluctance to extend credit in times of crisis. At the same time, positive short-term effects of counterbalancing measures may not come for free and the literature cautions about potential mid- to longer-term costs including misallocation of resources and the accumulation of bad loans.[32]

To the extent that many DFIs have been playing a more active role recently and that the European DFI landscape has been undergoing changes: what are the implications for DFIs, European banking and financial markets as well as for economic policy?

Promote and prosper or tough times ahead?

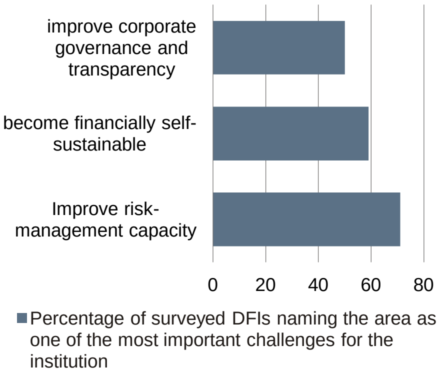
Some of the challenges that European DFIs face are similar to those of global peers. In addition, there are some issues specific to the European context. The following sections look at key challenges from three perspectives, i.e. i) considering DFIs themselves, ii) implications for European banking and financial markets as well as iii) economic policy.

Managing risks and DFIs' evolving role

Sound risk management is particularly important for DFIs because i) they often operate in areas where risks are higher, ii) they have concentrated exposures (in specific sectors for example) or iii) the types of risks they deal with are more difficult to predict, e.g. when financing projects with a long-term focus or infrastructure. A strong emphasis on sound risk management therefore partly follows from their business model.

[31] For recent developments concerning the EU investment plan also see Focus Europe (5 June) and Global Economic Perspectives (4 November).
[32] See for instance Bertray et. al (2012).

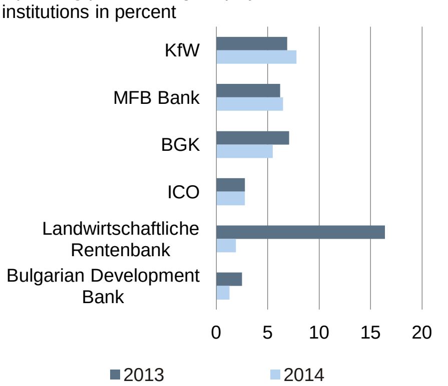
Key challenges for DFIs - globally 21



Sources: De Luna Vicente/Martinez (2012), Deutsche Bank Research

Most European DFIs profitable 22

Operating profit/average equity for selected institutions in percent



Sources: Fitch (2015), Deutsche Bank Research

Their countercyclical activities intensify demands on risk-management for European DFIs because they imply an extension of risks in terms of scale and scope and navigating an environment of considerable uncertainty. For DFIs this means organisational and procedural challenges, in the sense that they need to be able to scale up if needed and have adequate processes to flag and deal with risks accompanying this. To that extent, risk-management capacity at DFIs also has implications for the economy at large.

Balancing a countercyclical role for DFIs with the notion of having lean institutions focused on “gap-filling” can be a challenge both in terms of organisation and governance of DFIs. For example simple capacity constraints can limit quick up-scaling. At some point, the “gap-filling only” and strong balancing roles could therefore even be contradictory. Arguably the role definition is something that DFIs – being instruments of economic policy – cannot do completely on their own. Organisations’ capacity for risk management and sound governance, however, are key prerequisites to ensure that they can adapt flexibly to changing circumstances.

The literature on DFIs stresses that they can play a useful countercyclical role but cautions about potential negative mid-to longer term effects which can arise from not cutting back activity when it is no longer needed.[33] Here, the test for many European DFIs is yet to come.

European economies have been affected by the crisis to different extents, and their financial and banking markets differ considerably in terms of structure. Hence, there is no general answer to how active DFIs should (currently) be, when is the right time to scale back or where additional activity is still needed.

The empirical picture at the moment reflects this heterogeneity: Some DFIs (e.g. ICO and SID) have started to cut back activity, suggesting that they react flexibly to changing conditions. Others continue to have growth plans (e.g. some DFIs in CEE). – some of which are quite ambitious –Finally, newly established institutions are to some extent naturally scaling up (e.g. BPIfrance after reorganisation[34]) and establishing their role. At the European level, EFSI should work to support national DFI activity to some extent.

Several structural factors also suggest an extended period of greater DFI activity in Europe. First, the European banking sector is still undergoing restructuring. Hence, DFIs may step in where there are (perceived) gaps. At the same time, government funds are strained in many countries and hence DFI activity may be regarded as a preferred way to support economic activity and channel resources in a way that is rather market friendly in principle.

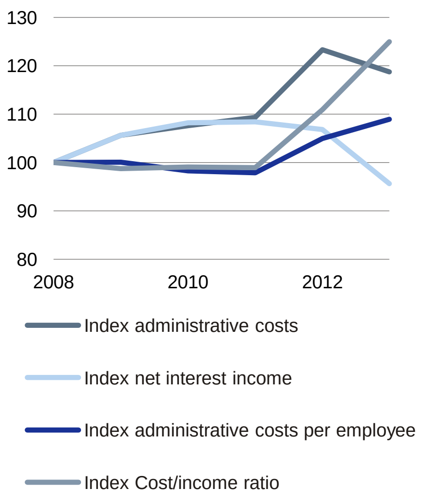
In some cases, extension of DFI activities may raise competition issues, particularly if institutions operate close to commercial banking. At the same time, there are recent examples where DFIs are actually being set up with the intention to foster greater competition on national banking markets (notably GB and IE). Again, given the heterogeneity of DFIs as well as national banking markets, the balance needs to be struck on a case-by-case basis, in keeping with basic single market principles.

The common European framework and competition rules may actually prove an advantage in this respect. While imposing limits on what DFIs can do, long-term experience suggests that DFIs work better within a more clearly defined focus and hence competition rules could help to avoid “overburdening”. At the micro-level, introducing temporary programmes and regularly (re)assessing tasks can help to support flexibility, but ultimately the quality of corporate governance plays a key role in ensuring that DFIs manage their (changing) tasks well.

[33] See for example Bertray et al. (2012).
[34] See Banque Publique d’investissement Plan stratégique 2014-2017.

German promotional banks: interest income declines, costs rise 23

Index 2008=100

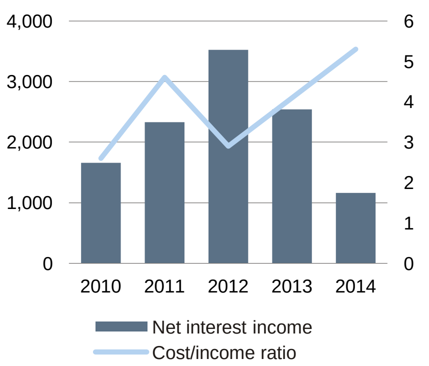


Averages for KfW and 9 subnational promotional banks

Sources: Annual reports, Deutsche Bank Research

Similar challenges for Italy's CdP 24

Left: Net interest income in EUR mn, Right: Cost/income ratio in percent



Sources: Cassa depositi e prestiti, Deutsche Bank Research

Profitability and Performance

DFIs do not operate with the main objective of maximising profits. Most European DFIs examined have been profitable recently, though (see graph 22).

Again, heterogeneity with respect to domestic economic conditions as well as business models restricts the scope for generalisations. However, recent developments suggest that interest income for a number of European DFIs is on the decline, reflecting the impact of the low-interest rate environment. In this respect, many DFIs show similarities with the commercial banking sector in some countries.

Another similarity is that costs have been increasing for many DFIs. This may result from a combination of extended activities, investments in bank infrastructure (digitalisation) as well as new regulation.

The combination of macroeconomic conditions and DFIs' business model may pose the biggest mid-term challenge for them, though. This concerns for instance the use of traditional promotional instruments in an environment of persistently low interest rates. At the same time promotional banking activities are also affected by the prospects and pace of the recovery in Europe, which impact on the risks and rewards for projects.

Again, quality of risk management and governance practices play a key role in ensuring financial sustainability at the micro-level. Some DFIs have also adopted minimum targets for profitability, which can help to foster sound performance.

Transparency, regulation and supervision

Transparency, regulation and supervision are key issues with regards to DFIs, particularly from a systemic perspective. It is helpful to distinguish between different types of transparency here.

1. Individual entities

European DFIs provide information about their organisations and business activities via the usual channels, issuing annual reports, information on their websites etc. Most of them also make some information available in English. Reporting reflects the respective national legal requirements, e.g. accounting rules being used or what other information needs to be included in annual statements. In addition, some of the larger DFIs that source parts of their funding on capital markets are also covered by rating agencies. Nevertheless, there is little standardised information on DFIs. In addition to financial information, DFIs also put an emphasis on informing about promotional activities; here, performance can be harder to capture, metrics vary and comparability can be limited.

2. European system of DFIs

Systemic transparency remains quite low, though, which is due to idiosyncratic structures of national promotional landscapes and organisational differences of institutions. For example, there is no transparent and easily comparable treatment of DFIs as a category across national (financial) statistics, which also limits possibilities for comparison across countries. This makes it hard to assess their role and significance for financial markets from a systemic perspective and to evaluate their role comparatively.

Greater Europeanisation of financial market regulation as well as common supervision in the Banking Union have not (yet) led to substantial changes in terms of systemic transparency because due to the differences between individual DFIs, supervision for them remains fragmented as well.

Some institutions are subject to ECB supervision (wholly or in part); others remain under supervision by national authorities. Some DFIs are not under direct ECB supervision but did take part in the stress-test by EBA/ECB in 2014, which is a positive signal in terms of enhancing transparency.[35]

On an international level, there is broad consensus that DFIs should be subject to regulatory and supervisory standards similar to private financial institutions wherever applicable.[36] With respect to design and treatment of DFIs for financial market regulation, preserving a level playing field between public and private financial institutions is important – not only with respect to the national level but also across countries. At the same time, promotional activities may sometimes warrant differential treatment requiring careful balancing when designing regulation.

Low systemic transparency partly reflects that DFIs have developed with a national (or subnational) focus as part of their financial systems over a long time. However, there are drawbacks to this patchwork in terms of higher information costs about promotional activities or programmes, for instance in the area of promotional financing for SMEs. Also, where promotional goals are very similar, limited comparability simply makes it harder to assess what works (best) and what does not. Arguably, this becomes more problematic, the greater the reliance on DFIs as an economic policy instrument.

Against this background, the proposed investment advisory hub and the project portal as part of the EFSI could help to identify and develop projects and facilitate access to information.

3. Choice of policy instruments

Finally, from an economic policy perspective, transparency with regard to governments using DFIs as a policy instrument is an issue. They can be a useful and actually market friendly policy instrument, working with private financial institutions or attracting private partners as co-investors for projects. However, there needs to be transparency on subsidy components and DFIs should not be used as a vehicle to circumvent budgetary constraints.

Cooperation and coordination

DFIs in Europe can be described as a multilevel system. Despite links, it is a system with heterogeneous members and rather limited cooperation or coordination. Hence, it remains a challenge how to leverage this system efficiently and minimise duplication and overlaps.

In addition to links via funding and associations such as the European association of public banks, of which many public financial institutions in Europe with promotional goals are members, a number of issue-based cooperations have been emerging. To the extent that many DFIs support similar goals – notably promoting SMEs or supporting long-term growth via investment in infrastructure – issue-based cooperation could potentially be intensified further.

There have also been proposals to move towards greater centralisation, for instance by creating a “Eurosystem of (public) investment banks” consisting of a federal fund (aka a restructured EIB) that would also coordinate the activities of national DFIs in the eurozone, thereby playing a key role in channelling funds and helping to increase long-term investment.[38] While promoting further cooperation – both among national institutions and with the EIB – seems

Statistical treatment of DFIs 25

To the extent that DFIs are an instrument to pursue economic policy goals, it is a question how they are treated in national statistics.

As a general rule, if financing decisions by DFIs require government endorsement or relevant governing bodies act under guidance of the government or are staffed with government officials, DFIs become “captive financial institutions”. In this case, their lending and borrowing needs to be included in national accounts.

If lending decisions are taken at arm’s length from government and governing bodies are independent, lending and borrowing is generally accounted for outside government statistics and outside the scope of the Stability and Growth pact.

Because governments can play different roles in the economy (owner of financial assets, acting for public policy purposes, implementing the budget), accounting for transactions between government and public corporations is not always straightforward and often requires case-by-case consideration of the type of entity and the specific transaction. In the EU, Eurostat provides general guidelines and advice to Member States.

For detailed information see Manual on Government Deficit and Debt – Implementation of ESA 2010.

Sources: European Commission, Eurostat (2014), Deutsche Bank Research

Issue-based cooperation among DFIs in Europe 26

— NEFI – a network of institutions in Europe that promote SME-financing, established in 1999.

— The Long-term Investors’ Club (LTC) in which institutions pursuing long-term investment activities interact. Founded by the EIB in 2009, LTC includes both European and non-European members.

— Six major European financial institutions joined forces in 2008 to establish a common equity fund – Marguerite – for infrastructure investments.

— At the European level, the project bond initiative by the European Commission and the EIB aim to support investment in infrastructure.[37]

Source: Deutsche Bank Research

35 Slovenian SID and KfW Ipex.
36 See for instance de Luna-Martinez/Vicente (2012) and Basel Core Principles for Effective Bank Supervision.
37 See Eric Heymann (2013) for an overview.
38 See Valla, Brand and Doisy (2014).

worthwhile, the question remains whether to pursue this using a bottom-up or top-down approach.

Contributions to EFSI 27

Eight EU member states have so far pledged contributions to EFSI via their national promotional banks.

— BG: EUR 100 m (June 2015)
— SK: EUR 400 m (June 2015)
— PL: EUR 8 bn (April 2015)
— LU: EUR 80 m (April 2015)
— FR: EUR 8 bn (March 2015)
— IT: EUR 8 bn (March 2015)
— ES: EUR 1.5 bn (February 2015)
— DE: EUR 8 bn (February 2015)

In addition, the UK has announced that it will make a guarantee available to co-finance infrastructure projects in the UK (not via promotional bank).

Sources: European Commission (2015), Deutsche Bank Research

Top-down approaches, i.e. a more centralised system, are likely to have some drawbacks. Aside from whether there would be political consensus for a centralised system, at an organisational level it could have costs in terms of information collection about the local market situation. There, more decentralised systems are likely to have an advantage, which can make it easier to identify suitable projects but also to ensure that DFI activity addresses local market failure. In practical terms, a more centralised system that coordinates European DFIs top down also has the problem that there are not “similar units” across member states; which raises the question of how to deal with different entities and systems across member states. Against this background, a bottom-up approach that strengthens cooperation among existing entities and comparable information about them seems more sensible.

The establishment of the EFSI could help to strengthen cooperation among DFIs and the EIB and help to promote investment. For example, the EIB (and the EIF) are able to provide guarantees to national DFIs, thereby indirectly supporting their investments. At the same time, the success of the EFSI is partly contingent on the participation of national (and subnational) DFIs who should for instance play a crucial role in identifying suitable projects in a short time frame. Up until now, several member states have pledged contributions to the EFSI via their national promotional banks. Also, a number of national DFIs have announced projects to be financed as part of the EFSI. Yet it is too early to evaluate both the effectiveness of additional instruments and the cooperation between the European and national promotional institutions at this point. While certain best practices and principles for DFIs at an individual level have been suggested, for instance on governance structures, transparency etc., there is no blueprint for structuring cooperation between entities in a multi-level system.

EFSI – where do we stand and what are next steps? 28

— June 2015: adoption of the EFSI regulation, involving also a redeployment of funds from other EU pools (“Connecting Europe”, “Horizon2020”).
— July 2015: European Commission announces further steps to get EFSI up and running including a Communication on national promotional banks and their role in supporting the investment plan, a delegated act for a Scoreboard of indicators to underpin the selection of projects, and final arrangements to start the European Investment Advisory Hub (EIAH) and the European Investment Project Portal (EIPP).
— The EIAH, a single access point offering advice and technical assistance to facilitate project development, and the EIPP, i.e. a web portal providing information about investment projects in the EU, are in the process of becoming fully operational.
— A number of projects have already received EFSI support. These include infrastructure projects, e.g. wind-farms in Belgium, renewable energy projects in France or Denmark, a clean energy R&D project in Spain, as well as support for programmes to boost entrepreneurship in Germany. EFSI financial support includes both equity participation and loans.
— June 2018: Completion of the EFSI investment programme, followed by EFSI evaluation including the role of and cooperation among national promotional banks.

Sources: European Commission (2015), Deutsche Bank Research

Again, DFIs and better cooperation among them can help with respect to policy goals such as promoting long-term investment or financing for SMEs – but it is no silver bullet. DFIs at member state and European level have a complementary role, can provide financing and help to improve the functioning of markets. Yet to the extent that barriers to cross-border investment or access to finance rather stem more from differences in rules and the lack of financial market integration, their impact is limited. Connecting DFI activity closely to the wider regulatory agenda to strengthen market-based financing and improve the functioning of markets, for instance through efforts to build a capital markets union, therefore seems a sine qua non.

Concluding remarks

DFIs have been a longstanding feature of banking and financial markets in Europe, helping to promote economic growth and support structural change in economies. The financial and economic crisis in the EU triggered enhanced activity by DFIs and also led to discussions about their role.

Given the current economic environment and changes on Europe’s banking and financial markets, DFIs are likely to continue playing an important role in the next years. Rather than crisis support, their focus is going to shift (back) to supporting structural change in economies. Here, they can play a useful complementary role focusing on areas of market failure. Market failure is not static though and in some cases there are alternative ways to address problems. To that extent, it remains an ongoing challenge to strike a balance between competition and promotion in DFIs’ relation with traditional financial service providers.

Risks lie with potential “overburdening” of DFIs and setting expectations too high on what they can achieve. DFIs can help to support economic policy goals but they are no substitute for reforms and certainly not a panacea. Similarly, having a DFI can be helpful tin mitigate the impact of a crisis – but does not prevent it from happening.

In spite of European DFIs’ heterogeneity, there are some “universal principles” – based on European and international experience – that contribute to the success of DFIs, notably strong risk management, clearly defined mandates, sound corporate governance as well as their regulation and supervision. While these principles apply primarily to individual DFIs, they also ensure that development banking in Europe works from a systemic perspective.

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Appendix

The table provides an indicative mapping of DFIs. It is not an exhaustive list of EU Member States' promotional financial institutions or promotional policies. The mapping should be treated with caution in light of the variety across member states and changes over time.

AT	aws (Austria Wirtschaftsservice GmbH) manages most public support schemes. aws is the product of a merger of different public entities in 2002; its predecessor (BÜRGES Förderungsbank) was founded in 1954. The focus is on promoting the development and financing of companies; main instruments are grants, loans and guarantees. It also operates a fund to provide equity (aws Mittelstandsfonds) and offers services to support new companies (business angels). In terms of programmes and services, aws offers inter alia small loans, loans to support investment in technology, loans to start-ups and guarantees for SME-microcredit. In addition, there are programmes to promote innovation, internationalisation and investment with a client focus beyond SMEs. As a special credit institution, Österreichische Kontrollbank (1946) also has a mandate to provide export credit insurance.
BE	Belgium has a decentralised promotional landscape reflecting its federal structure. A national fund to support SMEs (Fonds de participation) is being liquidated and competencies have been transferred to several regional institutions instead. Similarly, there are regional housing funds. Funds work with different financing partners including commercial banks in Belgium.
BG	Bulgarian Development Bank (BDB) was founded in 1999 and is a development and commercial bank. The focus is on financing projects of national or regional importance, agriculture, supporting SMEs and their internationalisation and growth of export-oriented companies. BDB offers services directly and indirectly and provides loans, guarantees, microfinance, and advisory services. The bank has two main subsidiaries, i.e. the national guarantee fund (loan guarantee scheme tailored to commercial banks) and a microfinance company.
HR	HBOR, i.e. the Croatian Bank for Reconstruction and Development, was established in 1992. It is the national development and export bank and export credit insurer. Its main focus is on promoting national economic development via different financing programmes. HBOR supports SMEs, infrastructure projects, tourism, industry, agriculture, environmental protection and exports. Products and services include loans and guarantees (for liquidity and new technology projects), insuring export transactions and providing business advice. Croatian Credit Insurance, a company owned by HBOR, provides credit insurance related to the selling of goods and services in Croatia and abroad. In addition, a separate agency (Hamag Investment), is engaged in SME promotion, administering regional funds.
CY	Cyprus Development Bank (CDB) was set up as a public development bank in 1963 but was privatised in 2008. There is a fund dedicated to promoting entrepreneurship as well as several regional investment agencies.
CZ	Czech-Moravian Guarantee and development bank (CMZRB) was established in 1992 and mainly focuses on supporting SMEs. It also participates in the realization of state policies by financing specific projects (improvements in technical infrastructure or housing). CMZRB offers guarantees, preferential loans and financing subsidies, as well as other banking services. It also acts as the manager of loan and guarantee schemes funded from structural funds (ERDF), state budget, regional budget or other sources. To promote the internationalisation of companies, it also cooperates with Czech Export Bank, a specialized banking institution to support exports.
DK	Denmark has a number of different public entities and financing institutions to support specific goals rather than one national DFI. Kommunekredit aims to provide cheap financing to support Danish communities. There is also a bank with a dedicated focus on agriculture (Landbrugets Finansieringsbank). The Danish Growth Fund is a state investment fund to promote the creation of new companies. It invests in equity and provides loans and guarantees for small as well as medium-sized enterprises in collaboration with private partners and Danish financial institutions.
EE	Founded in 2001, KredEX is the Estonian financing institution helping enterprises develop quicker and expand more safely to foreign markets. It offers loans, venture capital, credit insurance and state guarantees. It also offers loan guarantees for purchasing homes, as well as loans, guarantees and grants for solutions aimed at energy efficiency. The Estonian Development Fund (Arengufond) is a public institution to support positive changes in the national economy through investment activities, development monitoring and growth programmes. It invests in innovative companies seeking to grow, facilitating entrepreneurships and start-ups and the green economy.
FI	Finnvera was founded in 1999 by merging two promotional entities (Kera and the Finnish Guarantee board). It is a specialised financing company supporting Finnish enterprises and the Export Credit Agency of Finnland. It offers loans, loan guarantees, venture capital investments, export credit guarantees and other services associated with the financing of exports.
FR	Banque Publique d'investissement (BPI) was established in 2012 and is the product of the merger of OSEO (agency for SME development), CDC Entreprises (private equity arm of Caisse des dépots et Consignations), FSI (strategic investment fund) and FSI Régions. BPI aims to promote innovation, the seed stage, development, and internationalisation, transformation and transfer/buy-out of companies, by contributing to the financing of companies via loans and own funds. BPI is a financing company with two arms, i.e. Bpifrance Financement and Bpifrance Investissement. Caisse des dépots et consignations (CDC) acts as a long-term investor in the French economy, traditionally managing funds in regulated saving accounts. CDC participates in national economic development via its subsidiaries and invests in regional and local development together with public authorities.

DE	Kreditanstalt für Wiederaufbau (KfW) was established in 1948. It conducts promotional activities in Germany (supporting new companies, SMEs as well as promoting energy-efficient housing and financing for local infrastructure) and activities with an external focus (KfW IPEX providing export and project financing and DEG development bank focusing on promotion of developing and transition economies). While KfW is the main DFI in Germany, there is a sectoral development bank, Landwirtschaftliche Rentenbank (founded in 1949), that focuses on the promotion of the agricultural sector and rural development. In addition, there are regional promotional banks (Landesförderbanken) supporting economic development in their respective regions.
GR	In 2014 the Institution for Growth (IfG) was launched. IfG is an investment fund helping to pool financial resources from private and public organisations to provide financing for SMEs and public investment projects.
HU	Magyar Fejlesztési Bank Zártkörűen Működő (Hungarian Development Bank, MFB) is a Hungarian development bank originally founded in 1991. MFB is a specialised credit institution and the only participant in the Hungarian banking system which considers the promotion and modernization of the Hungarian economy its primary task. The objective of the Bank is to enhance investments and development, to bridge gaps in infrastructure, encourage growth of Hungarian businesses (primarily SMEs) both in Hungary and abroad, to stimulate technological and environmental development, energy efficiency and employment and contribute to Hungary's competitiveness in the international context through its activities. MFB is structured as a group comprising entities offering financial and investment services as well as managing public assets.
IE	Strategic Banking Corporation Ireland (SBCI) is a new institution to promote the development of the Irish economy and particularly provide support to SMEs. It offers investment and working capital loans, agricultural investment loans as well as facilities to refinance loans from banks exiting the market. Programmes are made available through on-lending with partners.
IT	Cassa depositi e prestiti (CdP) was founded in 1850. CdP manages Italian postal savings which are used to finance investment in infrastructure, investments by public entities and promote Italian companies (SMEs as well as strategic companies). Further activities include export and housing finance. CdP is a main shareholder in many major Italian companies. There is also a partly state-owned fund investing in risk capital of established SMEs as well as regional institutions to promote economic policy goals, e.g. Finlombardia.
LV	The DFI structure in Latvia has been undergoing changes recently. Latvian Development Financial institution (ALTUM) operated in the area of support programme implementation as a structural unit of Hipoteku banka, but separately from commercial services. It was then split off and started operating as an independent DFI in 2014. Plans to establish a single development institution by merging ALTUM, the Latvian Guarantee agency and the Rural development fund are planned to be completed in 2015.
LT	Invega is a public body dedicated to promoting SMEs and their access to finance. It provides different types of loans and guarantees, as well as venture capital, working with partner banks to implement promotional measures. Invega Fund is dedicated to implement the EU's JEREMIE initiative.
LU	Societé Nationale de Crédit d'investissement (SNCI) was founded in 1978 and is a public-law banking establishment that specialises in medium and long-term financing of Luxembourg-based companies. SNCI's financing instruments are investments in fixed assets, innovations and exports. It may also finance investments by Luxembourg companies abroad. SNCI offers start-up loans, equipment loans, medium- and long-term loans and there is a venture capital company providing equity.
MT	Malta is evaluating whether to establish a new national DFI.[39] Currently, Malta Enterprises is the national development agency which aims to promote international investment in Malta, also providing support to Maltese businesses.
NL	There are a number of promotional schemes and funds (e.g. Innovation Fund, Qredits – a microfinance institution) to support SMEs. In addition, Netherlandse Watershapsbank (NW) is a financial service provider for the public sector. Founded in 1954 it arranges short-term and long-term loans for water boards, municipal authorities, provinces, social housing, healthcare, educational institutions, Public-Private-Partnerships ("PPP") and activities in the field of water supply and the environment. Bank Nederlandse Gemeenten (BNG) is a specialised financing institution for the public sector established in 1914. BNG provides customised financial services ranging from loans and funds transfers to consultancy, electronic banking and investments for local authorities, public sector housing, healthcare and educational institutions and public utilities.
PL	Banka Gospodarstwa Krajowego (BGK), Poland's state-owned development bank, was founded in 1924. Its primary business objective is to provide banking services for the public financial sector, particularly by supporting government economic programmes (national as well as local and regional) implemented with the use of public funds. The state treasury and BGK are also significant shareholders in PKO bank, Poland's largest retail bank (also supports Marguerite).
PT	Portugal has recently founded the Instituição Financeira do Desenvolvimento (IFD). IFD is funded by the Portuguese state and European Structural and Investment Funds (ESIF). The focus is on facilitating SMEs access to funding (debt, equity and quasi-equity). IFD will manage and channel European Structural and Investment Funds allocated to Portugal, as well as reimbursements from ESIF-funded programmes.[40]

[39] See http://www.timesofmalta.com/articles/view/20150413/local/studies-underway-on-malta-development-bank.563792
[40] See Commission Press release http://europa.eu/rapid/press-release_IP-14-1214_en.htm

RO	Romania's EXIM bank, founded in 1992, is a specialised bank which supports the Romanian business environment via specific products (funding, guarantees and insurance). EXIM group includes EXIM bank and EXIM insurance-reinsurance company. There is also a national credit guarantee fund for SMEs (aecm).
SK	Slovak Guarantee and Development Bank (SZRB), established in 1991, is a specialised state institution focused on supporting business, particularly SME's. SZRB provides guarantees to start-ups and bank loan guarantees for SMEs. In addition, SZRBs also carries out other economic policy goals, e.g. financing for municipalities' projects, as well as renovation of housing stock. There is also a national agency for development of SMEs, i.e. Slovak business agency (until 2014 National Agency for Development of SMEs) to promote starting and developing businesses.
SI	Slovenska izvozna in razvojna banka (SID) is the Slovene Export and Development Bank established in 1992. The main activity provided on its own account is financing of business transactions in the area of SMEs (increasing competitiveness and internationalization), research, environment, supporting public institutions and municipal infrastructure. In addition, acting on behalf of the state, SID Bank provides export credit services, investment insurance and interest rate equalisation programmes. There is also a Slovene regional development fund.
ES	Instituto de Credito Oficial (ICO) is a state-owned bank attached to the Ministry of Economic Affairs and Competitiveness via the State Secretariat for Economy and Enterprise Support. ICO is both a state financing agency and a promotional credit institution that lends to SMEs. ENISA is a public company attached to the Ministry of Industry, Energy and Tourism that aims to facilitate funding for innovative business projects.
SE	Almi is the major actor to support SMEs in Sweden. Almi operates on a commercial basis and receives no regular government funding. There is a fund to provide venture capital to SMEs with high growth potential that seek to compete internationally and a state-owned venture capital company with a dedicated regional focus investing in the North of Sweden.
UK	British Business Bank (BBB) was launched in 2013 and aims to facilitate financing for SMEs and provide business advice.[41] BBB operates with three subsidiary arms (mandated, services, and commercial) that provide different services. UK Green Investment Bank, founded in 2012, is a state-backed infrastructure bank that aims to facilitate financing for green projects.[42] There is also a UK Innovation investment Fund operating as a fund-of-funds to create highly skilled jobs and drive technology investment as well as regional development agencies (e.g. Scottish Investment Bank and Co-investment Fund).
Sources: Company reports and websites.	

For further information on SME finance in different member states see http://ec.europa.eu/enterprise/policies/finance/guide-to-funding/indirect-funding/index_en.htm
and

Orcun Kaya (2014): SME financing in the Euro area – new solutions to an old problem.

For further information on trade finance export credit insurance see for instance International Finance Ltd/European Commission (2012): Study on short-term trade finance and credit insurance in Europe.

On municipal financing see for instance Frank Zipfel (2012): Einer für alle, alle für Einen – Kommunale Finanzagentur – ein Überblick.

[41] See European Commission Press Release: http://europa.eu/rapid/press-release_IP-14-1160_en.htm
[42] See European Commission Press Release: http://europa.eu/rapid/press-release_IP-12-1110_en.htm

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