EIB/OeNB Workshop
Investment and investment finance: The Austrian case

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Oesterreichische Nationalbank
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Summary

The OeNB and the European Investment Bank (EIB) jointly organised a workshop „Investment and investment finance: The Austrian case" at the OeNB on 20 March 2017. The aim of the joint OeNB/EIB workshop was to discuss strengths and weaknesses of Austria as a place for firms to invest and to identify areas where the EIB and other institutions can best support investment activity in Austria without crowding out other investment. Speakers from research institutes, from national and international institutions and practitioners shed light on various aspects of the topic. The most important findings of the workshop are as follows.

Austria has one of the highest investment shares of GDP in the EU, but it has been declining since the 1990s. Whereas the decline of the gross investment share (incl. depreciation) is mild, the net investment ratio dropped significantly since the year 2000, pointing to a substantial increase of the depreciation rate. The decline of the investment share in the last decades can be explained by lower long-term growth prospects − with demand being the main driver. The structure of investment in Austria is more favourable to growth than in the EU, as the share of all components of investment in GDP (except dwellings) is above the EU average, especially for investment in intellectual property. Nevertheless, Austrian firms seem to invest slightly less than the EU average in developing products that are new to the global market. Despite the high quality of the capital stock, which lies above the EU average, and a high capacity utilization rate, replacement and rationalization of production are main investment motives. Reasons for new investment are dominated by market outlook, innovation and digitalization. Firms mention bureaucratic obstacles ("red tape"), labour market regulations and skill mismatches as the main drags on investment activities in Austria.

The workshop also brought insights into investment finance. Internal finance is the most important and most stable source of funds for Austrian nonfinancial corporations. Longer-term banks loans increased while short-term financing by banks loses importance. On balance, banks in Austria are still tightening their credit standards. In this context, Austrian enterprises in particular regard the banks' collateral requirements and covenants as restrictive. Insufficient collateral was cited as the main reason for rejected or reduced loans to SMEs. However, from a macroeconomic point of view, research by the OeNB does not point to sizeable negative effects of loan supply on investment in Austria in the recent past. According to a practitioner's view, external financing is hampered by excessive bureaucratic and regulatory burden on businesses in Austria.

The EIB currently mainly provides finance for the Austrian transport, energy and SME sectors. For 2017, the EIB is targeting an even higher lending volume in Austria than in 2016, with a strong focus on EFSI (European Fund for Strategic Investments) activities. In line with

market needs and country aspirations, the EIB focus in 2017 is aimed at projects that strengthen Austria's ability to innovate by reallocating resources towards high-tech sectors and supporting innovative SMEs, transport, the health sector, energy efficiency and municipal infrastructure.

P. Mooslechner (Member of the Board, OeNB) and **D. Revoltella** (Director, Economics Department, EIB) held the opening remarks. P. Mooslechner regarded the workshop as an important undertaking and he emphasized the need to focus on real investment as the main driver of economic growth and employment. He pointed to the long-lasting nature of the present crisis, which brought about weak demand, underutilized capacity, political uncertainty and subdued expectations about future economic growth. He concluded by emphasizing the role of European policymakers to help revive both public and private investment. The European Central Bank has done its part by lowering interest rates and providing liquidity to the banking sector which lead to favourable financing conditions for companies, thereby preventing even further drop in investment. D. Revoltella opened the workshop by recalling EIB's mission to support sound investments. In this regard, one of the objectives of the workshop was to identify areas where EIB can support Austria without crowding out other investment. The EIB Group Investment Survey (EIBIS) for Austria that was launched at the workshop could help identify such areas.

D. Ritzberger-Gruenwald (OeNB) chaired the first session on trends, forecasts, determinants and bottlenecks of investment in Austria. **Martin Schneider** (OeNB) kicked off the presentations by outlining the stylized facts. Austria has one of the highest investment shares on GDP in the EU, but it has been declining since the 1990s. The structure of investment in Austria is more favourable to growth than in the EU, as the share of all components of investment on GDP (except dwellings) is above EU averages. The decline in investment share in the last decades is justified by lower long-term growth prospects – demand being the main driver. OeNB's research does not point to any negative effects of loan supply shocks on investment in Austria recently. Looking forward, it seems that the current investment cycle peaked in 2016 and is expected to slacken from early 2017 onward. In comparison to the previous cycles, the duration of the current investment cycle is similar, the magnitude is on the upper range and the composition is similar to 2011, with transport and ICT equipment as main drivers (unlike the previous cycles when machinery investment used to be the main driver).

D. Revoltella presented the EIB Group Investment Survey for Austria. The survey supports the growth story of investment in Austria, with a history of strong investment activity, confirmed over the crisis. Infrastructure investment held steady throughout the crisis at times when many other EU countries went through fiscal consolidation that entailed also public investment cuts. In Austria, this was supported by creative infrastructure financing model, particularly for transport. R&D investment, and recently machinery and transportation investment (regulatory induced), have been the main drivers of investment activity in terms of asset type. The survey points to high and expanding investment in Austria and high quality of the capital stock, based on firms self-assessment. However, Austrian firms seem to be investing slightly less than EU average in developing products that are new to the global market and are more focused on tangibles. This requires further push for innovation. While replacement remains the investment priority of Austrian firms, high capacity utilization is pushing particularly medium/large firms and firms in manufacturing to consider capacity expansion. Business and labour market regulation and skill mismatches were cited by the firms as main drag on investment. External finance is less binding than for the EU as a whole, although collateral requirements of banks are an issue for some firms. Austrian firms more than the EU average use at least 50% of internal funds to finance their total investment. Austrian firms rank among the top in the EU in terms of share of firms that invest abroad.

With increasing costs associated with cross-border business models, supporting Austrian firms in their cross-border challenges will be important.
W. Hoelzl (WIFO) looked at investment in Austria from the perspective of the WIFO Investitionstest, a tool for forecasting and nowcasting investment in Austrian manufacturing sector. Firms' investment motives in the current year are dominated by replacement and rationalization of production. On balance, the two main factors influencing investment for the current year and next year are technological change and demand.
To conclude the first session, **W. Waschiczek** (OeNB) discussed the role of finance in corporate investment in Austria. In line with the EIB Investment Survey, he pointed out that internal finance is the most important and most stable source of funds for Austrian nonfinancial corporations. Annual growth of longer-term loans has increased while short-term financing by banks loses importance. The share of firms reporting that they have "no need for bank loans" is almost 80% of the surveyed firms. On balance, banks in Austria are still tightening their credit standards, in comparison to the euro area average that reports slight easing. Overall loan demand increased last year for the first time since the crisis but remains weaker than the euro area average. Austrian SMEs regard the banks' requirements on collateral and covenants as restrictive. For all Austrian firms financing obstacles have diminished since their peak in mid-2015, although credit constraints are less likely for larger firms than for small and medium sized enterprises.
A. McDowell (Vice President, EIB) opened the second session by thanking the Österreichische Nationalbank for co-organizing with the EIB the event and offering the opportunity to have such a high level and insightful debate. Such discussion is valuable and important for an institution like EIB in better understanding market gaps and areas where EIB can best bring value. The discussion also gave a lot of room for optimism for Austria, given the high investment activity and high quality of capital stock. Focusing on identifying the remaining investment gaps and bottlenecks in Austria is therefore even more crucial, and the EIB Investment Survey is an important tool in this regard. Looking at the investment activity in Austria through the EIB Investment Survey lens, the EIB/EFSI should remain supportive of the further push for innovation, risk sharing products and PPP projects, as well as education, communication and utilities infrastructure, and of the Austrian firms' cross-border challenges. For 2017, the EIB is targeting even higher lending volume in Austria than in 2016, with a strong focus on EFSI activities. In line with market needs and country aspirations, the focus in 2017 is aimed at projects that strengthen Austria's ability to innovate by reallocating resources towards high-tech sectors and supporting innovative SMEs, transport, health sector, energy efficiency, municipal infrastructure and education.
E. Gnan (OeNB) chaired the second session on enhancing investment in Austria. Following-up on A. McDowell's outline of EIB's plans in Austria, **F. Palanza** (EIB) gave an overview of EIB Group activities in Austria. EIB total exposure to Austria stood at 4.4% of Austrian GDP (EUR 15.3bn) as of end-2016, with a strong presence in the transport, energy and SME sectors. Main counterparts have been public sector entities and financial intermediaries. Over the last five years, transport, telecommunications, SMEs and energy (mainly renewables) have been the main recipients of EIB loans in Austria. Over the same period, EIF committed EUR 663m, aimed at raising EUR 1.9bn in risk financing for SMEs. Loans to innovative companies and social entrepreneurs played a role in 2016 EIF activity. EIB lending activity in Austria in 2016 (EUR 1.447m in signed loans) was dominated by transport and telecommunications sectors. In 2016, the EIB approved EFSI operations of EUR 190m in Austria, hereby mobilizing total investments of EUR 490m.
Ch. Schneider (WKO) gave a business perspective on the investment environment in Austria and outlined some policy recommendations. He emphasized that the focus should not be on enhancing investment but on creating an environment conducive for investment. He started by pointing to the significant drop in the net investment ratio since the year 2000, more than 60%. This is a result of inflexible depreciation methods, resulting in "old assets on

the books". WKO's own investment survey showed that small companies have on balance negative expectations of economic climate for the next 12 months, and both small and to some extent medium companies have on balance negative expectations of investment volume and number of employees. Investment activity mainly serves maintenance and only rarely comprises new investment projects. 21 % of surveyed firms have no investment plans. Companies in manufacturing show more positive expectations for the next 12 months than those in services. Reasons for new investment are dominated by market outlook and innovation and digitalization. Reasons against new investments refer to no investment needed, and overall uncertainty. In answering the question as for which framework conditions would be necessary as incentive for investments, the largest number of firms pointed to further reduction in non-wage labour costs. In order to improve the investment environment, Mr. Schneider recommended reducing corporate income taxation (and introducing other targeted investment incentives), including flexible depreciation methods in the Austrian tax code, further reduction of non-wage labor costs in the medium-term, cutting red tape, and increasing investment in intangibles to keep up with the digitalization of the Austrian economy.

B. Sagmeister (AWS) discussed the collateral squeeze and access to finance by Austria companies. Tighter regulatory requirements on bank capital led to higher collateral requirement, shorter maturity of loans provided by banks as well as to avoidance of smaller projects (SMEs, start-ups). For Austrian SMEs, the share of rejected and reduced loans increased considerably since 2009. Insufficient collateral has been cited as the main reason for rejected/reduced loans. This collateral squeeze can lead to less innovation, less growth and eventually to loss of competitiveness of Austrian SMEs. To tackle the collateral squeeze, AWS has introduced a guarantee instrument backed by the Austrian state and targeted for domestic investment, internationalisation of Austrian firms, venture capital and SMEs. The guarantee instrument includes variations with and without state aid. The highest impact of guarantees was seen for innovation-oriented enterprises. Due to favourable economic effects and positive impacts on companies the Austrian Federal Government recently increased the volume of new guarantees for SMEs. In addition, AWS guarantees have been co-financed by EIF since 1998.

U. Schuh (BMWFW) outlined recent and ongoing initiatives of the Austrian Federal Government to stimulate investment in Austria. The government recently introduced a bonus for additional investment for SMEs and for large enterprises as well as a bonus for additional employment. The government has continued stepwise reduction of non-wage labour costs since 2014. He also spoke about government's activities in supporting investment in construction (including residential housing), broadband infrastructure, and R&D. In terms of firms' access to finance, besides the AWS initiatives, he mentioned targeted programmes for start-ups and crowdfunding initiative focusing on small scale issuances and investments.

N. Zimmermann (Berndorf AG) provided an entrepreneur's perspective on Austria as a business location. He summarized it in one phrase: "great history, doubtful presence, great future". He commented on excessive bureaucratic and regulatory burden on businesses in Austria. After the crisis, the relationship between banks and firms has changed. The regulatory changes in banking created an environment where borrowing arrangements with banks now pose much more administrative burden on firms than before. Entrepreneurial banking has evolved into a sector overwhelmed by mistrust of corporate management. His company, Berndorf AG, and many other firms are now turning more and more to internal sources of finance in order to limit their dependency on banks. In addition, administrative burdens and auditing costs are affecting firms' recourse to the stock market, as initial public offerings have become increasingly burdensome even for medium sized companies.

The presentations can be found at https://www.oenb.at/en/Monetary-Policy/Research/workshops.html