

European Bank for Reconstruction and Development (EBRD)

FY2002 Appropriation	FY2003 Scheduled Request	FY2003 Arrears Request	FY2003 Total Request
\$35.8M	\$35.8M	\$26,238	\$35.8M

For FY2003, the Administration requests appropriations of \$35.8 million for paid-in capital for the sixth of eight payments under the capital increase agreement of the European Bank for Reconstruction and Development (EBRD) and \$26,238 to clear one-third of outstanding arrears.

The EBRD promotes private sector development and entrepreneurial initiative in former centrally planned economies in Central and Eastern Europe, Russia, and the former Soviet Union. Borrowing countries are expected to be “committed to and applying the principles of multiparty democracy, pluralism, and market economies.” The Bank also has a mandate to promote environmentally sound and sustainable development.

Key Facts

- EBRD was created in 1991 to promote private sector development, foreign investment, privatization, and efficient financial markets in Central and Eastern Europe and the former Soviet Union.
- The U.S. is the single largest shareholder in the EBRD with a 10.2% share following the Bank’s 1996 capital increase. In 2001, U.S. contributions to the EBRD totaled \$35.8 million.
- Since inception, the EBRD has financed a total of \$17.9 billion in loans and equity investments, helping mobilize a total of \$60 billion in investment in the region. The EBRD committed a record \$3.2 billion of business in 2001 compared to 2000 commitments, which totaled \$2.4 billion. EBRD disbursed over \$2 billion in 2001, a 67% increase over 2000.
- EBRD’s focus on private sector development continues: roughly 76% of its portfolio is invested in private sector projects, well over the Charter requirement of 60%. EBRD develops the private sector through loans and equity investments in private sector projects and by mobilizing private capital alongside its own resources.
- The EBRD also provides public sector loans, with and without sovereign guarantees, to promote development of market-oriented economies through commercialization and/or privatization of state-owned enterprises and public utilities. The EBRD also focuses its operations on project finance, ensuring the revenues from the projects in which it participates can repay the investments made.

Recent Policy and Program Developments

Information Disclosure

- In July 2001, the first review of the public information policy took place and indicated areas for improvement on compliance, such as timely public disclosure of country strategy papers once they are approved by the Board of Directors and timely posting of project summary documents in advance of Board consideration of projects. As a result, the U.S. and other donors requested a review in 2002 of the policy itself. The U.S. also continues to push to make environmental assessments for “category A” projects in the private sector available at least 120 days prior to a Board vote. The current policy only requires they be made publicly available 60 days prior to a Board vote, which does not comply with the U.S. legislative requirement.
- In July 2000, the Bank approved a new public information policy, which is posted on the Bank’s website (www.ebrd.com). The new policy requires the Bank to disclose its sector policies in draft and inviting comments, country strategy papers, project summaries, and environmental impact assessments. Environmental impact assessments for public sector projects are required to be in the public domain for at least 120 days prior to Board consideration.

Post Conflict Assistance

- In 2001, the Federal Republic of Yugoslavia became a member of the EBRD and over the course of the year, 11 projects were approved with a value of \$230.6 million. EBRD has continued work on development of a Balkan Regional Action Plan and involvement, along with other IFIs, in the work of the High Level Steering Group (HLSG). The EBRD makes a special effort in Serbia and Bosnia, in particular, to ensure that its resources are used appropriately.

Efficient and Effective Use of Financial Resources

- EBRD is an efficient and cost-effective institution that, except for losses caused by the Russian financial crisis in 1998, has recorded profits, with which it has built reserves, every year from 1995 through 2001. The Bank has had nine consecutive budgets with no real increase in administrative costs and is committed to maintaining tight budget control, even in the face of increased lending volume.
- EBRD uses a productivity indicator to gauge its own “organizational performance”. This indicator measures productivity based on the weighted average of new annual commitments and portfolio per administrative expenditure and is tracked by the Bank over time.

Efforts to Improve Internal Controls

- The first Chief Compliance Officer was hired in 2000 to promote good governance and ensure that the highest standards of integrity are applied to all Bank activities. Recently, a

new Officer was hired and will begin work in early 2002. Key areas of focus for the Chief Compliance Officer include:

- Ensuring that the actions of EBRD staff, management, and members of the Board of Directors are ethical and consistent with the Code of Conduct.
 - Oversight of Bank management and staff on proper management of actual and potential conflicts of interest with respect to the Bank's clients and other concerned parties.
 - Selection of project sponsors that meet appropriate standards of ethics and integrity.
- At the Genoa Summit in 2001, the G7 Finance Ministers report on Strengthening the International Financial Institutions and the MDBs recommended that all MDBs have an independent inspection mechanism to enhance internal governance, accountability, and transparency. The EBRD does not have such a mechanism and the U.S. Executive Director and her G7 counterparts have requested that the EBRD establish such a mechanism.

Efforts to Improve Borrower Governance

- EBRD continues to work with both public and private clients to improve governance through increased transparency, accountability and incorporation of specific governance requirements into projects, such as externally audited financial statements. Where EBRD takes an equity stake, it sits on management and supervisory boards to add direct governance and oversight.

Monitoring and Evaluation

- EBRD regularly evaluates projects for their success in creating transition impact, improving the environment, and maintaining sound investment principles. The Bank's Project Evaluation Department has created a substantial database of operations assessments evaluating "lessons learned" for EBRD staff. Since 1993, when the Bank began evaluating its projects, 74% of its projects have been assessed as having a "high" transition impact. The U.S. carefully reviews projects with a focus on holding the EBRD to a high standard of demonstrating its financing will maximize transition.

IFI Collaboration

- In the year to June 2001, the EBRD mobilized almost \$2 billion in cofinancing, 55% from commercial sources and 45% from official sources. Other IFIs such as the IFC, European Investment Bank, World Bank, MIGA, Nordic Investment Bank and the Islamic Development Bank providing roughly \$400 million of this joint finance and export credit agencies accounted for \$23 million in cofinance.
- The EBRD has also coordinated with other IFIs, such as the World Bank, on private sector development in Southeastern Europe under the Stability Pact and more recently in Central Asia.

Environment and Energy Efficiency

- The Bank's policy and guidelines cover sustainable use of natural resources, environmental oversight, information dissemination, and public participation. All new projects require adherence to relevant European Union and/or World Bank environmental standards.
- Environmental assessments and public consultation are required for all environmentally sensitive projects and Country Strategies also include a review of local environmental issues. The U.S. has also recently requested a review of the Bank's current environment policy, which was approved by the Board of Directors in 1996.
- The Bank has worked extensively to improve environmental conditions in the municipal sector. In 2001, the EBRD provided over \$300 million in financing for fifteen projects with a total value of nearly \$900 million. The projects focused primarily on water supply, water-wastewater treatment, and municipal solid waste management. For example, in 2001 the Board approved a loan in rubles to the Russian city of Surgut that will focus on priority investments that reduce the city's operating costs and that finance general rehabilitation and upgrading of the municipal water and district heating systems in Surgut.
- The Bank also works to improve energy efficiency throughout its countries of operation both through its regular investments and through targeted investments in the energy sector. A recent example is a Lithuania district heating project designed to improve public sector energy usage. The project will bundle small energy efficiency projects that would otherwise not be financially viable into one loan administered through the Lithuanian Ministry of Finance.

Nuclear Safety

- The EBRD manages the Nuclear Safety Account (NSA) on behalf of the United States and other donor countries. The NSA provides grants to perform short-term safety improvements to the most dangerous reactors in the region linked with a commitment to their early closure.
- Since 1997, the EBRD has managed the \$700 million donor-funded Chernobyl Shelter Fund. This fund, which began issuing contracts in 1998, will assist in providing a new and safe sarcophagus for the damaged Chernobyl nuclear reactors. The last operating reactor at Chernobyl was closed in December 2000. (In December 2001, the Ukrainian authorities asked the EBRD not to consider a \$215 million loan for the completion of two nuclear power plants, K2 and R4.)

Core Labor Standards

- Since 1999, the EBRD has included labor issues in Country Strategies and the U.S. Executive Director works to ensure consistent treatment of relevant labor issues in Country Strategies as well as investment operations. Most of the Bank's countries of operation already

have in place laws that provide labor protections, and EBRD policy requires borrowers to comply with all national laws, including labor laws, in individual projects.

Opportunities for U.S. Business

- In 2000, the EBRD Board approved U.S. sponsored projects totaling over \$200 million in EBRD investment and \$676 million in total project cost. This represents almost 10% of the Bank's business volume in 2001, roughly equal to U.S. shareholding in the EBRD.

Supporting U.S. Objectives

Increasing Productivity

EBRD's focus on fostering the transition to market-oriented economies and promoting private and entrepreneurial initiative serves to increase capital and labor productivity.

- In some cases, EBRD projects directly increase labor productivity through investment or lending for updated technology or equipment. A small but illustrative example is a small ice cream company that used a loan from one of the EBRD's small business credit lines to purchase new assembly line equipment improving output from roughly 100 units per worker hour to nearly 1000 units per worker hour.
- In other cases, the impact is more indirect but still critical, as in the facilitation of credit to small and medium-sized enterprises (SME) through financial intermediation. For example, the EBRD may provide a credit line to a local bank to enable it to on-lend to SMEs in a country where such financing would not otherwise be available.

Combating Terrorism

- EBRD has expressed a clear commitment to support efforts to combat terrorism and is cooperating with the U.S. and the UN in that regard. At the request of the U.S., the Bank is putting in place additional due diligence procedures to ensure that none of its funds inadvertently go to terrorists or their agents.

Regional Priorities

Contribution for the EBRD Small and Medium Enterprise (SME) Support Fund

- Using funding provided under the Support for Eastern European Democracies Act (SEED Act), the U.S. Treasury established a fund at the EBRD in July 2000 to support SME financing through technical assistance to local financial institutions and credit lines for on-lending to SMEs. To date, the program has received \$10 million from the FY2000 SEED Act to support countries in Southeast Europe and \$11 million, including \$1 million allocated specifically for Serbia, from 2001 SEED Act Funding. In 2002, the Administration will expand the program to Freedom Support Act countries.

- The U.S. contribution will leverage an additional \$100 million of EBRD financing to financial institutions for on-lending to SMEs. The program supports three main activities: 1) debt finance to SMEs by on-lending through eligible banks; 2) technical assistance to train credit analysts and promote sound business practices and good governance at participating banks; and 3) technical assistance to identify legal, regulatory and policy impediments to improve the operating environment for SMEs.

Russia Small Business Fund (RSBF)

- Established in 1994 as a ten-year fund with a pledged contribution of \$150 million from the EBRD and the same amount from donor countries (the G-7 and Switzerland), RSBF has been successful in reaching businesses and generating on-lending, supporting 61,000 loans totaling \$647 million, but has not yet become fully sustainable. U.S. has contributed \$36.5 million and is planning to provide additional financing.