Transforming Markets

A Development Bank for the 21st Century

A History of the EBRD

Volume 2

Andrew Kilpatrick and **Anthony Williams**

Transforming Markets

A Development Bank for the 21st Century

A History of the EBRD

Volume 2

Andrew Kilpatrick
and
Anthony Williams

Central European University Press
Budapest–Vienna–New York

© European Bank for Reconstruction and Development
One Exchange Square
London EC2A 2JN
United Kingdom

Website: *ebrd.com*

Published in 2021 by
Central European University Press
Nádor utca 9, H-1051 Budapest, Hungary
Tel: +36-1-327-3138 or 327-3000
E-mail: ceupress@press.ceu.edu
Website: www.ceupress.com

This work is licensed under
a Creative Commons Attribution-NonCommercial-NoDerivatives 4.0 International License.

Terms and names used in this report to refer to geographical or other territories, political and economic groupings and units, do not constitute and should not be construed as constituting an express or implied position, endorsement, acceptance or expression of opinion by the European Bank for Reconstruction and Development or its members concerning the status of any country, territory, grouping and unit, or delimitation of its borders, or sovereignty.

ISBN 978-963-386-474-6 (hardback)
ISBN 978-963-386-411-1 (paperback)
ISBN 978-963-386-412-8 (ebook)

Library of Congress Cataloging-in-Publication Data

Names: Kilpatrick, Andrew, author. | Williams, Anthony, author.
Title: Transforming markets : a development bank for the 21st century : a history of the EBRD : Volume 2 / Andrew Kilpatrick and Anthony Williams.
Description: New York, NY : Central European University Press, 2021. | Includes index.
Identifiers: LCCN 2021033664 (print) | LCCN 2021033665 (ebook) | ISBN 9789633864111 (paperback) | ISBN 9789633864128 (ebook)
Subjects: LCSH: European Bank for Reconstruction and Development--History. | Development banks--Europe. | Economic development projects--Europe.
Classification: LCC HG3881.5.E83 K55 2021 (print) | LCC HG3881.5.E83 (ebook) | DDC 332.1/53--dc23
LC record available at https://lccn.loc.gov/2021033664
LC ebook record available at https://lccn.loc.gov/2021033665

Table of Contents

List of Abbreviations VII
Acknowledgments XIII
Foreword by Odile Renaud-Basso, President of the EBRD XVII
Preface 1

PART I An Evolving Landscape
Chapter 1 Pivot to Turkey 7
Chapter 2 Markets in Crisis 45
Chapter 3 Arab Spring 85
Chapter 4 Operations in Greece and Cyprus 123
Chapter 5 Geopolitical Tensions 155

PART II Towards Sustainable Market Economies
Chapter 6 Rethinking Transition 197
Chapter 7 Equality of Opportunity 241
Chapter 8 Supporting Resilience and Good Governance 269
Chapter 9 A Better Climate 337

PART III The Role of the EBRD
Chapter 10 The EBRD after 30 Years 403

Photos 441
Index 457

List of Abbreviations

AfDB – African Development Bank
ADB – Asian Development Bank
AEB – Agreement Establishing the Bank
AFG – High-Level Advisory Group on Climate Change Financing
AKP – Justice and Development Party (Turkey)
ASB – Assistance to Small Business programme
ATCs – assessment of transition challenges
ATQs – assessment of transition qualities
BAAC – Budget and Administrative Affairs Committee
BAS – Business Advisory Services
BAT – best available technology
BEEPS – EBRD-World Bank Business Environment and Enterprise Performance Survey
BEERECL – Bulgarian Energy Efficiency and Renewable Energy Credit Line
BIDSF – Bohunice International Decommissioning Support Fund
BOC – Business Ombudsman Council
BOI – Business Ombudsman Institution
CBR – Central Bank of Russia
CDU – Central Democratic Union of Germany
CEB – Central Europe and the Baltics
CESEE – Central, Eastern and South-eastern Europe
CGAP – Corporate Governance Action Plan
CIDA – Canadian International Development Agency
CIF – Climate Investment Fund
CIS – Commonwealth of Independent States
CMD – Capital Markets Development
COO – country of operations
CONIA – Cairo Overnight Index Average (interest rate)

COP – Conference of the Parties
COP13 – Thirteenth meeting of the Conference of the Parties
COP15 – Fifteenth meeting of the Conference of the Parties
CP – Commercial Paper
CRR – Capital Resources Review
CSE – Country and Sector Economics
CSG – Client Services Group
CSRF – Country Strategy Reporting Framework
CSRM – Country Strategy and Results Management
CTF – Climate Technology Fund
DCFTA – Deep and Comprehensive Free Trade Area
DCK – Democratic Choice of Kazakhstan
DfID – UK Department for International Development
E5P – Eastern Europe Energy Efficiency and Environment Partnership
EaP – Eastern Partnership
EBRD – European Bank for Reconstruction and Development
ECB – European Central Bank
ECOFIN – Economic and Financial Affairs Council, of the European Union
EEC – European Economic Community
EIB – European Investment Bank
EMEA – Europe, the Middle East and Africa
ESP – Environmental and Social Policy
ETC – Early Transition Country
ETCF – Early Transition Country Fund
ETI – Expected Transition Impact
EU – European Union
EU-NIF – EU Neighbourhood Investment Facility
EU-PHARE – Poland and Hungary Assistance for the Restructuring of the Economy
ExCom – Executive Committee
FI – Financial Institution
FOPC – Financial and Operations Policies Committee
FSB – Financial Stability Board
FVP – First Vice President
FX – foreign exchange
GAP – Gender Action Plan
GB – Garanti Bankasi (Turkey)

G7 – Group of Seven countries (Canada, France, Germany, Italy, Japan, the UK and the USA)
G8 – Group of Eight countries (Canada, France, Germany, Italy, Japan, Russia, the UK and the USA)
G20 – Group of Twenty (Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Republic of Korea, Mexico, Russia, Saudi Arabia, South Africa, Turkey, the UK, the USA, and the European Union)
GCAP – Green City Action Plan
GCF – Green Climate Fund
GEF – Global Environment Facility
GEFF – Green Energy Financing Facility
GET – Green Economy Transition
GIS – Green Investment Scheme
GPA – Governance and Political Affairs
HLRM – High-Level Reporting Mechanism
IA – Integrated Approach
IC – Investment Council
ICGI – Investment Climate and Governance Initiative
ICMA – International Capital Market Association
ICR – Insolvency and Creditor Rights
IDLO – International Development Law Organisation
IsDB – Islamic Development Bank
IEA – International Energy Agency
IFC – International Finance Corporation
ILO – International Labour Organization
IMF – International Monetary Fund
INDC – Intended Nationally Determined Contributions
IPA – Instrument for Pre-Accession Assistance
IPCC – Intergovernmental Panel on Climate Change
IRENA – International Renewable Energy Agency
ISDA – International Swaps and Derivatives Association
JIAP – Joint IFI Action Plan
JNA – Joint Needs Assessment (for Georgia)
JOLE – Journal of Labor Economics
KIDSF – Kozloduy International Decommissioning Support Fund
KKB – Bank TuranAlem (later renamed BTA Bank) and Kazkommerzbank

LC2 – Local Currency and Local Capital Markets Development
LDR – loan-to-deposit ratio
LIBOR – London Interbank Offered Rate
LITS – Life in Transition Survey
LSE – London School of Economics and Political Science
LTP – Legal Transition Programme
LTT – Legal Transition Team
MBR – Millennium Bank Romania
MDA – Multi-Donor Account
MDB – Multilateral Development Bank
MDG – Millennium Development Goal
MENA – Middle East and North Africa
MFA – Republic of Turkey Ministry of Foreign Affairs
MidSEFF- Mid-size Sustainable Energy Financing Facility
MMWG – Money Market Working Group
MosPrime – Moscow Prime Offered Rate
MoU – Memorandum of Understanding
MRV – Monitoring, Reporting and Verification
MSME – micro, small and medium enterprises
NATO – North Atlantic Treaty Organization
NBG – National Bank of Greece
NDC – Nationally Determined Contributions
NDEP – Northern Dimension Environmental Partnership
NGO – non-governmental organisation
NPL – non-performing loan
OCDS – Open Contracting Data Standard
OCE – Office of the Chief Economist
ODA – official development assistance
OECD – Organisation for Economic Co-operation and Development
OE&E – Operational Effectiveness and Efficiency
OGC – Office of the General Counsel
OpsCom – Operations Committee
OSCE – Organisation for Security and Cooperation in Europe
OSG – Office of the Secretary General
PPA – Power Purchase Agreement
PPO – Priority Policy Objective
PPP – public-private partnership

PPP – purchasing power parity
PTI – Portfolio Transition Impact
3R – Reduce, Reuse, and Recycle
R&D – research and development
RAROC – risk-adjusted return on capital
RFR – risk-free rate
RLC – Revenue Loss Coverage
ROISfix – RUONIA Overnight Interest Rate Swap
RUONIA – Rouble Overnight Index Average (interest rate)
SBS – Small Business Support
SCCF – Special Climate Change Fund
SCF – Strategic and Capital Framework
SDG – Sustainable Development Goal
SEE – South-eastern Europe
SEFF – Sustainable Energy Finance Facility
SEI – Sustainable Energy Initiative
SEMED – southern and eastern Mediterranean
SGI – Strategic Gender Initiative
SIDA – Swedish International Development Cooperation Agency
SLOVSEFF –Slovak Sustainable Energy Financing Facility
SMEs – small- and medium-sized enterprises
SoE – state-owned enterprise
S&P – Standard & Poor's
SPCom – Strategy and Policy Committee
SPREF – Southern and Eastern Mediterranean Private Renewable Energy Framework
SRI – Sustainable Resource Initiative
SSA – Sub-Saharan Africa
SSF – Shareholder Special Fund
STEM – Science, Technology, Engineering and Mathematics
SUAL –Siberian-Urals Aluminium Company
TAM – TurnAround Management
TAMBAS – TurnAround Management and Business Advisory Services
TCX – Currency Exchange Fund
TEB –Turk Ekonomi Bankasi
TFP – Trade Facilitation Programme
TFP – total factor productivity

TIBR – Tbilisi Inter Bank Rate
TLREF –Turkish Lira Overnight Reference Rate
TurSEFF – Turkey Sustainable Energy Financing Facility
UNCITRAL– United Nations Commission on International Trade Law
UNFCCC – United Nations Framework Convention on Climate Change
URA – Ukraine Reform Architecture
VISP –Vital Infrastructure Support Programme
VP3 – Vice Presidency, Policy and Partnerships
WiB – Women in Business
WTO GPA – World Trade Organization's (WTO) Agreement on Government Procurement (GPA)
ZSE – Zagreb Stock Exchange

Acknowledgements

Volume 1 of the *History of the EBRD* was completed in March 2020, shortly after the Covid-19 pandemic imposed the first lockdown in the UK and many other countries. At the time, it was hoped—even without knowing whether vaccines would be successful—that life would be back to normal by the end of that summer. Preparations for Volume 2 began with that expectation.

More than one year later, the coronavirus is still present and continues to create pressures on the working lives of those with whom we talked during the course of writing this book. Our sincere thanks goes to them, the many people connected with the Bank, past and present, who have contributed in various ways to this second volume of the EBRD's history. The list is long so it is attached at the end of this note.

The current President of the EBRD, Odile Renaud-Basso, has lent her full support to the project which was first suggested by her predecessor, Suma Chakrabarti. We are heavily indebted to them both.

Writing a book in a "virtual" setting during a pandemic has been a challenging experience. We are fortunate that technological advances have allowed the task to be accomplished in time for the 30th anniversary year of EBRD operations. It certainly would not have been possible without the benefit of video internet platforms that by now have become commonplace. On that note, we should credit the scientists and engineers who have made this possible, and at the same time hope that we can soon return to face-to-face communication.

Writing and researching via remote access has its challenges, but these are small in comparison to the disruption faced by the world of publishing over the past year. Our heartfelt thanks go to CEU Press who have supported our endeavour throughout, and especially to Linda Kunos, Senior Editor.

We are grateful to Jonathan Charles, and especially to Jane Ross, who have stood valiantly behind the production of the book from the outset, to Nick Jacobs (Contributing Editor, GlobalCapital) for his editorial guidance, and to Norbert Seiler and Paul Kearney for detailed comments on the

manuscript. Alex Plekhanov and Peter Sanfey also provided helpful comments on chapters at various stages, along with Vanora Bennett and Axel Reiserer. Tea Gamtkitsulashvili supplied valuable statistical assistance and Anna Vasylyeva helped with some interviews. We thank them all.

Last, but not least, thanks are due to Maggy and Dawn for their forbearance and willingness to put up with many days of absence—albeit within the same home—while the book was put together.

Andrew Kilpatrick
Anthony Williams
London, 12 May 2021

The authors would like to thank (in alphabetical order) the following for their help, insights and assistance:

Sevki Acuner; László Andor; Memduh Ackay; Olga Aristeidou; Bengu Aytekin; Edward Bannerman; Anthony Bartzokas; Phil Bennett; Vanora Bennett; Erik Berglof; Russell Bishop; Catarina Bjorlin-Hansen; Harry Boyd-Carpenter; Jonathan Charles; Eirini Christodoulaki; Gian Piero Cigna; Alistair Clark; Joanna Conway; Hester Coutanche; Mike Davey; Friso de Jong; Milica Delević; Valeria Della Rosa; Boris Dincer; Dermot Doorly; Sabina Dziurman; Joe Eichenberger; Elisabetta Falcetti; Francesca Foglia; Anne Fossemalle; Harold Freeman; Hildegard Gacek; Tea Gamtkitsulashivili; Kristalina Georgieva; Susan Goeransson; Kristine Grun; Lado Gurgenidze; Sergei Guriev; Heike Harmgart; Adonai Herrera-Martinez; Peter Hjelt; Kemal Cagatay Imigri; Nick Jacobs; Beata Javorcik; Nigel Jollands; Gordon Jones; Matthew Jordan-Tank; Stephane Jucobin; Fani Kallianou de Jong; Paul Kearney; Natasha Khanjenkova; Franka Klingel; Libor Krkoška; Jacek Kubas; André Küüsvek; Hans Peter Lankes; Isabelle Laurent; Jean Lemierre; Vassili Lelakis; Oleg Levitin; Colm Lincoln; Francis Malige; Levan Mebonia; Nik Milushev; Gianpiero Nacci; Piroska Nagy-Mohácsi; Lucie Newman; Theresa Nierderle; Michel Nussbaumer; Lin O'Grady; Jonathan Ockenden; Aude Pacatte; Oksana Pak; Nandita Parshad; Akhil Patel; Steve Petri; Alain Pilloux; Alex Pivovarsky; Alex Plekhanov; Enzo Quattrociocche; Biljana Radonjic Ker-Lindsay; Artur Radziwill; Barbara Rambousek; Horst Reichenbach; Bojana Reiner; Axel Reiserer; Odile Renaud-Basso; Thomas Revial; Anastasia Rodina; Mattia Romani; Olga Rosca; Jane Ross; Alan Rousso; Charlotte Ruhe; Arda Sahinkayasi; Anna Sali; Peter Sanfey; Gerard Saunders; Norbert Seiler; Christoph Sicking; Ian Smith; Craig Spruce; Nick Stern; Juraj Strasser; Svetlana Strizovic; Josué Tanaka; Leander Treppel; Arvid Tuerkner; Jim Turnbull; Jan Willem van den Wall Bake; Axel van Nederveen; Anna Vasylyeva; Endrita Xhaferaj; Bryan Whitford; Jeromin Zettelmeyer; Nibal Zgheib.

Foreword

This second volume of the *History of the EBRD* is going to press just as the world is tentatively looking forward to a recovery from a pandemic that has cost hundreds of thousands of lives and dealt a devastating blow to economies across the globe.

Intense suffering has continued. There may still be further setbacks and, even in recovery, the world could look quite different from the pre-Covid-19 era. There is no doubt that the virus has wielded a disproportionately greater impact on the poorest and most vulnerable sections of society, including in the EBRD's regions.

The EBRD stands willing and prepared to stand by its countries as they continue to deal with the immediate challenges of the worst global health crisis in generations. It will help them deliver a more robust and more inclusive economic future once the recovery takes hold.

This second volume of the EBRD's history tracks the path that the Bank has taken over the last 15 years, during which it strengthened its contribution to the countries where it invests, making a greater impact on the lives of the people it serves.

It covers a period where the Bank became even more international in its shareholder base and adapted to address more comprehensively the global challenges of the 21st century. The Bank embarked on a period of expansion to geographies beyond the planned economies of its post-communist remit. Yet, it remained unerringly true to its fundamental purpose to support its countries of operations in their quest to become well-functioning, market-oriented economies.

Picking up the story in the latter part of the first decade of the new millennium, we see how the EBRD transferred the skills it had successfully built up in central and eastern Europe and seamlessly applied them first to Turkey and then further afield.

We track the EBRD as it filled a policy vacuum that emerged in the global financial crisis of 2008/2009, taking the lead in a response that staved

off the worst impacts of the sharpest economic downturn since the transition collapse, and stepping up financing just as the private sector retrenched.

Just as there were signs of embryonic recovery in eastern Europe, popular protests erupted across the Arab world, reminiscent of the 1989 quest for freedom from the communist yoke. The EBRD responded to appeals from the international community and from emerging new democracies and brought its talents to the Mediterranean shores of North Africa and the Middle East. Just a little later, it supported the economies of two eurozone members, Cyprus and Greece, whose financial sectors had been devastated by a fiscal and debt crisis.

The Bank's strong early contribution had been to support the integration of post-communist countries into the EU and to encourage all of them to build free market economies. The ease with which it shifted gear to reach out just as effectively to a different set of countries is testament to the high quality of the EBRD's central proposition. It demonstrated during this period the supremacy of the Bank's unique business model over the confines of geography or cultural and historical heritage. It is a business model that thrives because of its targeted market-driven focus and support for the drivers of economic growth. It is success built on a presence on the ground in its countries of operations that is unmatched by other development institutions.

The EBRD has established a winning combination that brings together sectoral and institutional expertise with teams of highly professional local staff with a profound understanding of the economies and the political dynamic in each of the countries it serves. This insight into politics and access to policymakers facilitates meaningful dialogue with both local and the central authorities at all levels of political influence, including the very highest. These are relationships that engender mutual trust and respect and also allow for candour in those periods that call for difficult messages.

The EBRD's ability to forge strong partnerships has been another important plank in its support for emerging economies, one outstanding example being its cooperation with the European Union and key bilateral donors to provide finance and technical assistance for the countries of the Western Balkans as they work towards further EU integration.

The EBRD's mandate and the goals that it enshrines have remained unchanged since the creation of the Bank in 1991. But it has deepened its endeavours and its contribution to transition in the light of experience and added to the toolkit it uses to achieve its goals. It has shifted the balance

between financial investment and policy engagement and placed a greater emphasis on support for policy reform that underpins economic progress and guarantees that the EBRD's ultimate contribution is greater than the sum of its individual projects.

Rejecting the binary notion of "state bad, private sector good", the EBRD fully acknowledges the crucial role the public sector must play in helping to create institutions and regulatory frameworks within which the private sector can flourish. The Bank has worked tirelessly and across multiple economic sectors to help authorities deliver the institutional evolution and adherence to the rule of law that attracts international and domestic flows of sustainable investment.

During the period covered by this second volume, the EBRD strengthened the criteria according to which it measures the success of its interventions in emerging economies to take account of the sustainability of its transformational efforts. It has remained committed to improving such qualities as competitiveness and integration—core activities of the early years—but put an even stronger focus on green transition, inclusion and governance, as well as resilience.

There emerged an increasing alignment between the EBRD's priorities and the international development agenda when, in 2015, the United Nations unveiled its 17 Sustainable Development Goals and there was near universal endorsement of the Paris Climate Agreement, which finally made a determined global effort to address the urgent challenge of climate change.

Having pursued a strong environmental agenda since its inception, the EBRD's own contribution to the Paris accords was now a pledge to raise the share of its green financing to 40 per cent of annual investments by 2020, and then subsequently to scale up further its ambitions to become a majority "green" bank by 2025.

Just as it had reacted with determination and agility to earlier external events like the financial crisis and the Arab Spring, deftly applying its skills to new challenges, the EBRD also responded decisively to concerns about the negative impacts of climate change and to fears that the fruits of rising prosperity were not being shared fairly across societies in its regions.

It remained true to its belief in the positive forces of multilateralism and its rejection of nationalism and protectionism. It did not want to reverse the tide of globalisation, but it wanted to make it more widely beneficial—to

help small businesses and entrepreneurs in its regions participate competitively and successfully in the global marketplace.

It increased its efforts to reach out to those who risked being stranded on the margins of economic progress with the introduction of a fully-fledged strategy of economic inclusion. Through its investments and policy work the Bank could ensure the greater integration of individuals—who were missing out through no fault of their own—into the jobs market and to the world of enterprise.

As the EBRD now looks forward to the post-Covid era and implements its strategy for the next five years, it has three clear priorities:

- It will deliver on its ambitious **green** economy targets, with plans to ensure that every one of its projects is aligned with the Paris climate goals by end 2022, and that over 50 per cent of its investments are "green" by 2025. It will not neglect its other traditional investment areas including small businesses, industry and energy and infrastructure, but financing in these sectors will be an integral part of the EBRD's pathway to a net zero emissions future.

- It will promote **inclusion** and equality of opportunity through access to skills and employment, finance and entrepreneurship, providing targeted support especially for women, young people and underserved communities and seeking to address imbalances that have been put into particular relief by the Covid-19 pandemic.

- It will accelerate the **digital transition** process, supporting a trend whose importance has only been highlighted during the lockdowns that have been imposed to stem the spread of the coronavirus.

In the future, if this is what shareholders decide, the EBRD may determine whether there is scope for incremental further expansion of the Bank's geographic remit into sub-Saharan Africa and Iraq. We aim for a decision next year.

In the meantime, the EBRD remains a robust and reliable partner for all of its countries of operations.

It will make good on its pledge to deliver a stronger, sustainable economic future that changes lives for the better and is shared by the many, not just the few.

Odile Renaud-Basso
President, European Bank for Reconstruction and Development
May 2021

Preface

The EBRD was created at a time of momentous political and economic change. It would probably never have existed had it not been for the grand vision of Jacques Attali and his President, François Mitterrand, to push for a new European institution to help former communist countries embrace democratic values and market economics.

The fledgling institution symbolised a new Europe embracing east and west.

That perspective became more broadly based with the inclusion of OECD shareholders beyond Europe, at Mrs Thatcher's behest. And with it a combination of private and public sector standpoints. The Bank emerged as a well-balanced multilateral institution defined by its "European character," trans-Atlantic perspective and truly international shareholder base (spanning five continents).

Many of the EBRD's founders did not expect—or want—the institution to last for long. There was a widespread belief that while some assistance was needed to help markets become established in former command economies, once they were in place they would be able to guide economic progress without further interventions from development institutions.

This view proved to be wide of the mark. The transition towards market democracies was not an easy or straightforward process. The shocks from the radical changes to economic systems that occurred were severe and their effects long-lasting for the EBRD's countries of operations. The value of the EBRD's financial and other assistance thus became more durable than the more vocal market advocates had supposed at the start.

It was against this backdrop, described in Volume 1 (*After the Berlin Wall*), that the EBRD offered vital support in its early days to investors in central and eastern Europe and to local entrepreneurs seeking to develop their businesses and skills in the new market context. The EBRD soon grew to become a successful regional MDB with considerable sectoral expertise and developed a deep knowledge of countries in its areas of operations—in central, eastern and south-eastern Europe, Russia, the Caucasus and Central Asia.

At the halfway point of the EBRD's life, in the mid-2000s where this volume begins, the Bank was investing around €5 billion a year, more than double the rate seen at the end of the 1990s. It was also making substantial profits.

A vigorous debate was underway among shareholders and with the Bank's management over the size and future direction of the institution. It was prompted by the accession of eight countries of operations to the European Union, with two more slated to become member states in the near future. Arguments raged over the graduation of the EU countries. There was a further view that the EBRD, if it was to continue at all, should focus its investments towards the "south and east".

No-one predicted just how extensive and significant this 90-degree shift in geographic direction would turn out to be. Neither was it foreseen that the EBRD would double its balance sheet within 10 years.

It is the events and decisions behind the growth and reorientation of the EBRD that forms the basis of this volume. For much of this period, the quintessential "Bank for transition" also became a "Bank in transition". And it emerged the better for it.

The first part of the book depicts the geographic dimension of this change and includes the Bank's responses to the series of crises that contributed to these developments and the growth of its business.

After two decades of transition it had become clear—especially as a result of the global financial crisis—that successful market development went hand-in-hand with institutional development. Inadequate improvements to market-supporting institutions and wider governance issues were proving to be major hinderances in several of the EBRD's countries. Many countries had become stuck in transition.

Understanding the political economy of change proved to be just as important in the transition context as applying the tenets of market economics. This realisation prompted a review of the transition concept that underpinned the rationale for the Bank's activities.

The second part of the book looks at this and considers the implications of the review for the Bank's operational stance.

Transition was no longer just a matter of putting markets in place and investing to create a private sector. After all, by now markets and private sector activity were present almost everywhere in the EBRD's regions, albeit with varying degrees of success.

Instead, the view emerged that transition, and successful development, was more a matter of transforming these emerging market economies to be able to function well and become sustainable over the longer term. The transition story was thus a deeper and more complex one than simply introducing competition and integrating economies into regional and global markets, important though these were. It included a more prominent role for a (benign) public sector.

The core thesis was that transition could be better achieved by improving six qualities that together would transform a market economy to become sustainable, one which could grow steadily and prosper over the long run. Two qualities—"competitive" and "integrated"—were integral to the Bank's story so far. The other four—"resilient", "well-governed", "inclusive" and "green"—emphasised new or existing qualities that were regarded as additionally necessary for successful economic development.

The picture that was being drawn was coloured by circumstances that had arisen from the Bank's experience. The focus on resilience, for example, was a natural consequence of efforts to avoid a repeat of the damaging impacts from financial crises in the face of future economic shocks. The EBRD's work to improve local currency financing and strengthen local capital markets was one response.

Corrupt practices, the dominance of politically-connected cliques and the flouting of legal norms in several countries meant that the investment climate and business environment too often failed to support sound economic growth. To address this, the EBRD looked at ways to improve governance. Similarly, widespread and high levels of youth unemployment in southern and eastern Mediterranean countries put a spotlight on the need for better opportunities for young people. The striking inequalities facing women in this region, and also in Turkey, was another reason for an increased emphasis on inclusion by the Bank.

A further consideration involved a more complete integration of the Bank's green agenda within its transition apparatus. The EBRD was a pioneer in working with the private sector to tackle climate change and was playing a leading role in supporting a transition to a low carbon future. The rationale for focusing on green outcomes, as part of the systemic transformation needed to create a sustainable market economy, was strong.

From the beginning to the present day, the EBRD has focused on systemic change. As a relatively small IFI, it concentrated on building partnerships

through which it could achieve greater impact and change. Chief among them was its relationship with the private sector, where together with the EBRD substantial amounts of finance have been invested for transition and development.

This finance has been leveraged, especially in more recent times, through the Bank's policy engagements with public authorities and increased donor support to deliver structural reforms, enabling market improvements and greater investment and job opportunities. The EBRD's public-private partnership model has achieved a great deal and, in many ways, has been ahead of its time. The EBRD is a multilateral institution like no other.

The final part of this history looks at the role of the EBRD in this context. It takes a view of the Bank over the 30 years of its existence, including how its regions have fared over this time.

During this period, the EBRD responded rapidly and effectively to new challenges and circumstances. Although one of its original purposes—helping former communist countries develop a market orientation and a private sector—has faded with the passage of time, the logic of transforming economic systems to help countries become sustainable market economies has not. In fact, leveraging the private sector to deliver public goals, such as sustainable development or greater opportunities for women and young people, and encouraging the public sector to introduce market-supporting reforms has never been more important.

While the current predicament of trying to manage the spread of Covid-19 and address its economic consequences is of central importance, it will not be the only threat to development in the next 30 years. Among the most prominent that can be foreseen is climate change. Here too, the EBRD can make an important difference.

The balanced multilateral setting and public-private partnership model that has lain behind the EBRD's unique contribution to transition and development over the past 30 years is one that the global community would be well-advised to embrace.

The chances of longer-term success would appear to be greater if it does.

Andrew Kilpatrick
Anthony Williams
May 2021

Part I

An Evolving Landscape

Chapter 1

Pivot to Turkey

Introduction

In the autumn of 2008, the EBRD made one of the most important decisions of its then 17-year history. The Bank that had been set up specifically to support the countries of former communist eastern Europe voted to start investing in Turkey, a country without a communist past.

It was a controversial decision that saw three years of shareholder wrangling before a consensus could be reached. The debate surrounding accepting Turkey as a country of operations was sometimes emotional, with some fearing that by moving away from the post-communist sphere the EBRD was losing its soul and abandoning the rich heritage of a common cultural and historical past.

The discussion was also fiercely political, pitching key shareholders one against another. The notion that the EBRD would start financing projects in Turkey challenged the assumption that the EBRD's mandate was to perform a specific task in a clearly defined region and that it would close its doors on completion of that job. The USA and the United Kingdom, in particular, were initially firmly of the view that the admission of Turkey would overturn the very finite essence of the Bank's original remit.

The period leading up to the decision was one of intense debate among shareholders about the EBRD's future. Decisions over Turkey, and the geographic expansion it entailed, became intertwined with other key questions that divided shareholders at the time—the graduation of countries that became EU member states and payment of a dividend out of profits—both of which potentially constrained the Bank's forward path.

To any external observer, much of the discussion would have seemed arcane: an almost theological analysis of the EBRD's mission and a semantic dissection

of the meaning of "transition". Yet the debate struck at the very heart of the EBRD's purpose. Questions included whether operations in Turkey were compatible with the EBRD's transition and geographic mandate, and whether Turkey fulfilled the political and economic criteria to become a recipient.

According to one participant active at the Bank at the time, "We started having Jesuitical discussions—counting angels on the head of a pin, asking: What is transition? What is it to? What is it from?" Did transition refer only to the transition of former communist countries, implicit in the political context of its creation and the characteristics of every country it had ever worked in? Was transition restricted only to movement away from a communist command economy? Or was the mandate to promote the private sector, irrespective of the point of departure?

It was not that the EBRD had not faced membership issues before. One of the trickiest had been the only previous "out-of-area" expansion to Mongolia, a recipient since 2006. But this was not much help as a precedent for Turkey. Mongolia had not formally been part of the Soviet Union, but as a former communist state facing very similar transition challenges to its Central Asian neighbours it might as well have been.

The decision on Turkey was far more controversial because it threatened a change in direction and outlook for the Bank. Despite protestations to the contrary at the time, this is in fact what occurred. The pivot to Turkey turned out to have far-reaching consequences for the EBRD.

1. Turkey and the European Union

In the first years of the new millennium a major focus of the European Union (EU) was on enlargement and the accession of new member states. The EBRD had played an important role in bringing the former communist countries of central and eastern Europe to this point as part of its mission to integrate east and west.

Unlike its central European counterparts, Turkey was not a recipient member of the EBRD. It was a founding member. But it had long wished for a closer, more integrated relationship with the EU, which the new democracies to the north were now also seeking.

Turkey had in fact applied for association status with the European Economic Community as long ago as 1959, shortly after the EEC came into

being, and long before the former communist countries entered the fray. The Ankara Agreement of 1963, which promoted trade and Turkey's economic development, gave rise to the possibility of accession to the EC and ultimately to Turkey's membership. A Customs Union came into force in 1996[1] and the Helsinki European Council of December 1999 placed all candidates for EU membership, including Turkey, on an equal footing.[2]

Following a major financial crisis in 2000–2001, Turkey began a process of accelerated economic reform. An Accession Partnership with the EU was agreed in March 2001 and a national programme for the adoption of the EU Acquis was announced shortly afterwards. An election on 2 November 2002 resulted in the newly-formed Justice and Development Party (AKP), led by Recep Tayyip Erdoğan, coming to power. As a party with Islamist credentials this represented a significant change in Turkey's political make-up. Nonetheless, Erdoğan declared himself in favour of reform and Turkey's EU accession.

A few days after the election, former French President Valéry Giscard d'Estaing, who presided over the convention examining the constitutional future of Europe, offered some trenchant criticisms of Turkey's proposed accession to the EU in an interview reported in *Le Monde*. This received considerable prominence, and notoriety, with Giscard reported as saying, "Turkey is a country that is close to Europe, an important country ... but it is not a European country ... Its capital is not in Europe, it has 95% of its population outside"; and, as for enlargement outside Europe, "It is the end of the European Union!"[3] He advocated instead a partnership and cooperation arrangement, similar to the one the EU had with Ukraine.

Giscard was not alone in holding such views. According to *The Wall Street Journal* at the time, "Mr Giscard d'Estaing is the first top European official to say publicly what others have long said privately", in reportedly saying: "The majority of European heads of state and government have said they are against its joining the union ... 'but no-one ever told the Turks'."[4]

---

1 This was after an extended period of political instability in Turkey, including a military coup.

2 The candidates were (in alphabetical order): Bulgaria, Czech Republic, Cyprus, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovenia, Slovakia, and Romania. Following the launch of negotiations towards a 'just settlement' in Cyprus, Greece removed its threat of veto, allowing Turkey to be added to the list, making 13 candidates in total.

3 'For or against Turkey's Membership of the European Union', *Le Monde*, 8 November 2002.

4 Brandon Mitchener, 'France's Giscard d'Estaing Ignites EU-Turkey Debate', *The Wall Street Journal*, 11 November 2002.

Naturally, Turkish officials protested. In a letter to the former French President of the Republic, the Turkish ambassador to the EU, Oğuz Demiralp, argued: "Not only is Anatolia a part of classical Europe, but Turkey has also been part of Europe since the 10th century."

Despite various messages from senior EU politicians decrying the former President's remarks, the episode was damaging and brought to light a wider schism within Europe on Turkey. A lack of knowledge of the new government and concerns over progress on the political criteria added to the mixed views ahead of the 2002 Copenhagen European Council, which was due to take a decision on the accession of new member states, ten of which were EBRD countries of operations.

The Council agreed to conclude negotiations with eight countries so that they could become member states on 1 May 2004 and set a target of 1 January 2007 for the accession of two other countries (Bulgaria and Romania). But Turkey was not on the list. It was regarded as not having made as much progress as the others. The Council concluded that, if the Commission recommended it in one year's time, accession negotiations could begin then. According to one report, "uncertainty led the Copenhagen European Council … to postpone its decision on Turkish accession until December 2004, to the bitter disappointment of Erdoğan."[5]

Turkey continued to introduce reforms, but at the Brussels European Council in December 2004 a further delay to accession negotiations was announced stating they would start in October 2005. Cyprus had proved a sticking point as, in order to open negotiations, Turkey was required to recognise Cyprus as a member of the EU. This proved difficult. It was only later that the Turkish delegation agreed de facto recognition by signing a protocol to its customs union agreement with the EU to take account of the accession of the 10 new member states, which included Cyprus.[6]

It was not long after the Brussels summit that Turkey first showed interest in changing its status to become a recipient member of the EBRD.

---

5 Pierre Gerbet, 'The case of Turkey', p. 3, https://www.cvce.eu/obj/the_case_of_turkey-en-97eb9c0b-c49c-4111-86ab-52d33c5ece94.html

6 Gerbet, 'The case of Turkey', p. 4. The protocol was signed on 29 July 2005.

2. A Three-Cornered Problem

Management's dilemma

The accession of eight countries of operations to the EU raised questions over their future relationship with the EBRD. They were now firmly ensconced in a market-oriented economic system, one in which there was a strong commitment to multiparty democracy. To be sure, convergence was incomplete and gaps remained which the Bank could help to fill. But it appeared that the core goal of transition was to all intents and purposes complete. The ensuing period was marked by a debate over when and how these countries might graduate from investments by the EBRD, and this was the main preoccupation as preparations were laid for the next strategic capital review (CRR3) ahead of the 2006 EBRD Annual Meeting.

The EBRD President, Jean Lemierre, was in no doubt that graduation would be a mark of success for the EBRD. The institution had been created to assist the integration of east and west and for him "the great success of the EBRD, and it was acknowledged at the time, notably by the European Commission and by most of the shareholders, was that the EBRD had been very helpful in making the enlargement a success".[7] The strategy set out in CRR3 and endorsed by Governors in May 2006 made clear that these countries would graduate before the end of the decade.

Not all in management were as sanguine about the future as Lemierre appeared to be. The implications of the changes for the EBRD that lay ahead were serious. A loss of more than one-quarter of the Bank's countries of operations (by number) and a sizeable chunk of business volume for an organisation that had become used to growing rapidly, and successfully, was a potentially devastating blow.

The absence of eight EU countries, including further ahead potentially two more in Bulgaria and Romania, could have profound effects on the activities of the Bank as well as its balance. In 2004 and 2005, annual business investment in central Europe and the Baltics (CEB)[8] averaged 17 per cent of total volume, while Bulgaria and Romania accounted for a further 16 per cent. A hole ultimately approaching one-third of the Bank's business

7 Interview with Jean Lemierre, September 2020.
8 Excluding Croatia, which was part of the EBRD definition for the region at the time.

would not only dent profits severely, particularly as these countries were relatively profitable for the Bank, but it would inevitably mean a sizeable loss of staff and morale.

Graduation also had significant implications for the EBRD's abilities to fund rising investments in areas like the Balkans, eastern Europe and the Caucasus and Central Asia. In Poland, for example, the EBRD had invested hundreds of millions of euros that would generate revenue either from interest payments or from profitable equity sales that it would then funnel to new investments. These would no longer be available.

Intensified efforts in the Balkans or Central Asia, where the EBRD was now setting its sights, could help but would not be sufficient to take up the slack. Countries in these areas were generally smaller and more volatile and involved more difficult business environments than the EU accession countries.

Investments in the "south and east" of EBRD's existing region, though well-advertised and welcomed as a deepening of EBRD's transition model, could not solve the problem. The implication was that Russia would unavoidably become the mainstay.

Moscow was more than willing to fill the gap left by central Europe. Russia was already arguing that EBRD business volumes there were too low and was pushing for more. A diminishing presence of the EU countries provided the opportunity.

Indicative figures in the Bank's strategic preparations anticipated this change in direction. The plan showed the share of annual Bank business conducted in advanced countries dropping from 16 per cent in 2005 to 6 per cent by 2010, and a corresponding increase in Russia's share from 26 per cent to 41 per cent.

Geographically, and in terms of GDP, Russia dominated EBRD's region. But many in the Bank were apprehensive as to what heavy reliance on Russia implied for the management of the EBRD, including operating with a less-diversified portfolio. Some warned that increasing dependence on Russia was putting too many eggs in one basket.

At the same time, there were concerns about a growing number of individuals and companies in Russia with which the EBRD was unwilling to do business on account of integrity issues.

Some geographical expansion of the Bank began to look useful in this context. A glance at the map of EBRD's region, especially its south and east,

suggested countries like Turkey and Egypt and perhaps even the Middle East more generally—a vision that EBRD founder Jacques Attali had once entertained—could fit the bill. An important economy like Turkey's or Egypt's could provide an answer to this conundrum.

Turkey was in many ways the obvious choice. Egypt, like Turkey, was a founding member of the Bank and large enough, but it was poor, not as well connected to the region's markets and a sensitive proposition politically with then-President Hosni Mubarak in power. Further afield might have won support from some shareholders—the USA and the UK were keen for the international community to support Iraq's reconstruction, for example—but fault lines over the 2003 Iraq invasion were still fresh in people's memories and this would be a stretch too far.[9]

Turkey was different. It could claim European credentials. The notion of EBRD assistance fitted well with the idea of further European integration: not necessarily Turkey as an EU member state, but as a country with a significant and growing EU trading partnership—more than half its exports already went to the EU. It was the only original member in the region with a border with the EU that had not become a country of operations or an EU member state. And it was pursuing like-minded reforms to its central and eastern European neighbours, with a similar goal.

Besides, the operations side of the EBRD already knew Turkey well since many Turkish industrial conglomerates had been involved in EBRD financings over the past decade as they expanded into former communist territories.

Turkish partners included beer brewer Anadolu Efes that exported drinks to Kazakhstan, Moldova, and Russia and other countries in the region. With TAV, the airport group owned by Akfen Holdings, the EBRD had cooperated on the modernisation of airports in the Georgian cities of Tbilisi and Batumi; and the Bank had regularly worked with the glass manufacturer Şişecam in Bulgaria, Russia and Ukraine, as well as with numerous other Turkish companies. From the start of EBRD operations until 2009, Turkish companies were involved in €800 million of EBRD financing in the region.[10]

---

9 The Iraq invasion soured relations between those who chose not to be involved (most major European countries) and the "coalition of the willing". Many EU countries wanted nothing to do with the increasingly complicated situation the US-led administration faced in the country.

10 According to the Turkish Ministry of Treasury and Finance.

Straddling Europe and Asia, Turkey was an important hub for commercial links that supported the economic integration crucial to the long-term success of economic development across the EBRD's regions. In the view of one experienced senior banker, it was a "gateway to a wide and diverse region spanning Central Asia, the Western Balkans and the southern and eastern Mediterranean".[11] The sheer size of the Turkish economy meant that it had a tangible impact on other EBRD countries, whether in south-eastern Europe, the Caucasus or Central Asia. Any EBRD contribution to a strengthening of the Turkish economy would indirectly have a positive effect on these economies as well.

Entering a large, new market almost three-quarters the size of CEB would provide a neat solution to the potential problems that lay ahead, including the expected graduation of the EU-8 within five years.

For Lemierre, though, the key was to be found elsewhere: "The only way to convince people and to reassure people was to say 'No, there is a clear vision—which is accession to the EU. Let's do for Turkey what we have done for Poland!'"[12]

The advantages for the Bank's management were clear. But they faced a major dilemma. Although the EBRD was a regional development bank in the vicinity, it was not an ordinary development bank. It was a transition bank. It had been set up to help former communist countries adapt to democratic norms and develop market-based democracies. On the face of it, Turkey did not meet the EBRD's founding fathers' particular ambition for the institution.

Turkey's interest

While keen to encourage inward investment, Turkey had not hitherto revealed any desire to become a country of operations of the EBRD. It had never been part of the historic, communist genesis of the Bank; and the stigma of that era did not chime well with either the secular or Islamist perspective of modern Turkey.

Yet Turkey was clearly not shy about accepting finance from international financial institutions. And with accession negotiations at last on the

11 EBRD Press release, 21 April 2016. 'Turkey's journey to become the EBRD's largest market'.

12 Interview with Lemierre.

horizon, additional help could prove useful, particularly as the post-crisis economy continued to need structural support.

As well as being a founding member of the EBRD, Turkey had established long-standing relationships with international financial institutions. It had joined the International Monetary Fund (IMF) and World Bank as an early member in 1947, and was a recipient of World Bank and International Finance Corporation (IFC) loans for many years—by the mid-2000s it was the fifth-largest country in IFC's committed portfolio. The European Investment Bank (EIB) had been present in Turkey since 1965 and was a large investor, investing over €500 million in 2004 before ramping up activity to almost €1 billion in 2005, in preparation for Turkey's potential EU accession.

Turkey's 2000–2001 crisis had resulted in a US$ 19 billion augmented IMF programme that was now ending. The international financing together with a series of reforms, led first by Kemal Derviş (to 2002) and then Ali Babacan as Minister of Economy, had been a success. Turkey's economy was recovering well under the new government's programme with fast growth, averaging some 8 per cent a year, and inflation falling to a 30-year low.

However, concerns were mounting over a rapidly expanding current account deficit which by 2004 had reached 5 per cent of GDP—a level many saw as critical—leading to new discussions with the IMF. Given Turkey's volatile economic history the situation was still seen as fragile.

Turkey had a young and rapidly growing population and, despite a much-improved macroeconomic performance, structural deficiencies remained. Its GDP per capita of around US$ 6,000 was still a very long way short of most southern European countries. Turkey had also fallen behind central and eastern European countries: per capita GDP, almost 20 per cent higher than in Poland in 1991, was 10 per cent lower by 2003. By the turn of the millennium, Turkey had been surpassed by most CEB countries: its GDP per capita was one-fifth lower than the CEB average.[13] A relative lack of convergence with the EU was a source of disappointment for the authorities.

With a continuing goal of closer integration with EU countries against a backdrop of a need for further reforms and rising vulnerabilities ahead

13 In current US dollars, Turkey's per capita GDP was US$ 6,040 in 2004, and US$ 10,860 in purchasing power parity (PPP) terms. Per capita GDP in CEB was almost one-quarter higher and Greece, for example, was 2½ times larger in PPP terms.

of accession discussions, and facing growing objections within the EU to Turkish membership,[14] the Turkish authorities saw some value in enlisting the potential contribution of the EBRD. A number of the Bank's attributes supported this perspective.

An EBRD commitment to investing in the country offered a stamp of approval that would strengthen Turkey's ability to access international capital markets and mobilise other investors. This would help integrate Turkey into global and especially European financial markets. Turkish businesses—many of whose family owners were closely linked with the political authorities—would welcome the ability to access long-term finance where longer tenor private sector loans were in scarce supply.

Moreover, the Bank's skillset built on the back of helping transition economies—from its knowledge of privatisation, expertise in working with financial institutions and at the municipal level—was especially relevant to Turkey's needs. The fact that the vast bulk of EBRD finance was to the private sector and non-sovereign loans to the municipal sector was an added advantage.[15] As a multilateral with a majority European shareholding, there were policy routes that could also be explored.[16]

Meanwhile, in Paris and Berlin, and in Brussels, with mounting strains over the Turkish accession issue—especially in France ahead of the May referendum on the EU Constitution[17]—there was interest in additional opportunities to help Turkey and encourage reform. A view was emerging that the active involvement of the EBRD could assist the process. Discreet enquiries were made in the spring by the French and German offices at the EBRD on what might be needed for Turkey to become a recipient member.

---

14 Opposition parties in France and Germany were becoming more vocal on the issue. Angela Merkel, then opposition Christian Democrat Party (CDU) leader had already made plain that she did not believe Turkey could become a member "for the foreseeable future" and in December 2004 explained "that is why we are urging a privileged partnership with Turkey and not full membership" (*Suddeutsche Zeitung*, 16 December 2004). French President Jacques Chirac offered cautious support ahead of the May referendum, but kept open the idea of a "privileged partnership" as a fallback to full membership. (See 'Chirac envisages alternative to full EU membership for Turkey', *The Irish Times*, 3 December 2004.) His rival, Interior Minister and leader of the governing Union for a Popular Movement, Nicolas Sarkozy, was against accession: "There are two ways of associating [Turkey] to us: either by the status of social partner with Europe—which is rather my own way of thinking—or you integrate it, which is rather what I don't want." (BBC, 27 September 2004.) By mid-2005, attitudes had hardened further, see below.

15 In the period between 2000 and 2004, for example, about one-half of EIB's lending to Turkey was to the public sector.

16 A small additional advantage by switching to recipient membership was the possibility of obtaining a seat on the EBRD's Board. (This occurred later when Romania joined a constituency with Turkey.)

17 The French referendum was held on 29 May 2005, where the proposed EU Constitution was rejected.

According to the Turkish Ministry of Treasury and Finance[18], a letter from the Swiss Director who represented Turkey at the EBRD arrived in March informing them that a number of Directors at the EBRD were running with "the idea of Turkey's status change as a logical step forward" reflecting "Turkey's central geographical position in the EBRD region as well as EBRD's enabler position in the European Union (EU) accession negotiations". The letter emphasised that there would be "mutual benefits of the status change for both sides", with Turkey obtaining access to resources to help with its liberalisation and structural reform programme while the EBRD would find new investment opportunities.

The Turkish Ministry of Foreign Affairs (MFA) was also contacted that March, in this case by the EU Director at the EBRD, who pointed out that the Bank would have increased headroom for lending with countries expected to graduate soon and that the Bank was worried about consequential geographical concentration risks. Accordingly, it was possible that Turkey could become a recipient country if it desired to do so.

The MFA subsequently advised the Turkish Treasury to consider becoming a country of operations at the EBRD, and internal discussions among the Turkish authorities on the economic, political and foreign policy implications began.

In May 2005, following the successful conclusion of the earlier programme,[19] Turkey decided to consolidate its support from the IMF by agreeing a three-year US$ 10 billion Stand-By Arrangement. The IMF press release explained "the program aims to ... reduce the current account deficit to more sustainable levels" and "to create conditions for sustained growth ... [and] facilitate convergence towards the EU economies".[20] That same month, ahead of a technical framework for accession negotiations due from the European Commission in June, Erdoğan appointed Babacan as his chief negotiator for the upcoming EU talks scheduled for October.

Preparations did not go as smoothly as hoped, however. Turkey's refusal to recognise Cyprus when signing the customs union additional protocol at

18 This and the following two paragraphs are based on information supplied by the Turkish Ministry of Treasury and Finance, January 2021.

19 An initial stand-by credit of approximately US$ 3.7 billion was granted in late December 1999 to help bring down inflation and support the government's economic programme, and was followed by a US$ 7.3 billion Supplemental Reserve Facility in 2000 introduced in the face of declining market confidence.

20 IMF Press release No.05/104, 11 May 2005. 'IMF Executive Board Approves US$ 10 Billion Stand-By Arrangement for Turkey', 11 May 2005.

the end of July did not go down well. Towards the end of August, the French President, Jacques Chirac, voiced his concerns suggesting Turkey needed to recognise Cyprus before talks began. Simultaneously, Angela Merkel, who was about to be elected Chancellor of Germany, wrote to EU conservative heads of government to express her view that negotiations should not automatically lead to membership but be "open ended" and instead should involve a "privileged partnership". According to *The Guardian* newspaper, "the interventions by Mr Chirac and Mrs Merkel show that within weeks Turkey could face the nightmare scenario of losing the support of the EU's most significant countries."[21]

The Financial Times reported similarly on Friday, 26 August,

> Turkey's hopes for a smooth start to European Union membership talks on October 3 were shaken Friday by separate warning shots from France and Germany. … The prospect of Ms Merkel and Mr Chirac placing obstacles in the path of the Turks would be a huge setback for Ankara but would be in tune with public opinion in Germany and France, where opposition to Turkish membership is strong.[22]

The following Monday, 29 August, the EBRD President received a letter of the same date from the Turkish Governor, İbrahim Çanakçi, Undersecretary of the Treasury, requesting advice on a possible change of Turkey's EBRD status to become a recipient country. Referring to a bilateral discussion at the EBRD Annual Meeting earlier that year where, "we had the chance to consider at length the idea that has been flagged at the directorial ranks of the Bank regarding Turkey to be a country of operations …", Çanakçi asked Lemierre "to provide an assessment of the factors that would come into play in the case that Turkey becomes a country of operations for the Bank", and then set out some particular points of interest, such as the legal process, the advantages for Turkey's public and private sectors, and so on. Çanakçi concluded by saying he looked forward "to receiving your input to facilitate the discussions on the subject of a possible change of status".[23]

---

21 Luke Harding and Nicholas Watt, 'Turkey's EU dream dealt double blow as Chirac and Merkel raise doubts', *The Guardian*, 27 August 2005, https://www.theguardian.com/world/2005/aug/27/turkey.eu.

22 George Parker, Bertrand Benoit, and John Thornhill, 'Paris and Berlin dent Turkey's EU hopes', *The Financial Times*, 26 August 2005, https://www.ft.com/content/48584ff0-165f-11da-8081-00000e2511c8.

23 'Request for Turkey to become possible country of operation', 29 August 2005.

The President's reply on 15 September thanked Çanakçi for his letter and said a detailed response was in preparation and would be sent "as soon as it is ready". It appears no written reply was sent, but instead a visit by an EBRD delegation to Ankara was arranged to discuss the issues with the authorities in more depth and take the matter forward from there.

The Turkish request prompted a flurry of internal activity, particularly in the Office of the Chief Economist (OCE) and the Office of the General Counsel (OGC). Reviews of the economic, political, legal and operational aspects of the issues were swiftly launched under the umbrella of a Turkey Task Force involving senior officials from those departments and from the banking side.

An EBRD delegation led by the Secretary General, Horst Reichenbach, accompanied by the General Counsel, Deputy Chief Economist, a banking group director and others met with senior Turkish officials in Ankara in mid-October. The EBRD team explained management's thinking based on the internal paperwork prepared over the previous six weeks.[24] The EBRD Governor and his team responded with pertinent questions on legal, institutional and operational aspects related to recipient membership.

Sticking to their instructions, which had been to keep to low starting figures of €150 million for the first year and €300 million in the second, the team faced an awkward moment when Babacan asked what investment volumes the EBRD had in mind. According to one participant, Babacan scoffed at the mention of the initial amounts, commenting that he could obtain €150 million from one bank in a single transaction. Only when the quality of support the Bank provided alongside its investment projects was explained to him, and that the indicative figures were a small first step which would likely increase over time, was he reassured enough to carry on with the meeting. He found the EBRD's non-sovereign finance approach to municipalities and their utilities of interest, however.

Reflecting later on the experience, Reichenbach said "we went home with mixed feelings", but he concluded on balance that the Turkish authorities accepted the EBRD would add high quality investments to several industrial and financial sectors.

The President informed the Board on 26 October that the Turkish authorities had approached the Bank with queries on a change of status and proposed to share information on the legal and technical questions in a

24 The papers covered similar ground to the material that eventually reached Governors almost three years later.

closed session of the Board. He ventured that on the basis of the discussion a response to the Turkish authorities might then be prepared.

The opportunity to move towards operations in Turkey thus emerged in the context of EU accession and as a counterpoint to the expected graduation of some countries of operations. If the legal, technical and political barriers could be overcome it seemed only a matter of time before the move might be accomplished.

However, several major shareholders were uneasy at the prospect of Turkey becoming a country of operations. Some were ideologically opposed while others objected to a possible diversion of EBRD capital away from what they regarded as "higher priority" countries. The force of opposition was strong and problematic for Turkey which was keen to reach consensus if possible. Management's hands would be tied for the next two years.

Shareholder concerns

Preparations for the capital resources review to be agreed at the 2006 EBRD Annual Meeting were already well advanced by the time Lemierre informed the Board of Turkey's interest in a change of status. The big issues that had occupied management and Directors throughout the year had been how to deal with graduation and its implications and, to a lesser extent, pressure from Russia for a bigger share of the Bank's business.[25]

At the EBRD Annual Meeting in London in May 2006, shareholders acknowledged, "the historic achievements of the countries of central and eastern Europe in their economic and political transformation" and upheld the principle of graduation by declaring as part of the strategy "... the eight countries which have joined the EU will have graduated from the EBRD by the end of 2010".[26] Compromise on graduation had been achieved by accepting the argument that the EBRD would stop investing once it was no longer needed, while making clear at the same time that no country would be forced out from the EBRD against its will.

The five-year strategy paper proposed shifting the EBRD's focus to Russia, south-eastern Europe, the Caucasus and Central Asia. There was no

25 See Andrew Kilpatrick, *After the Berlin Wall: The History of the EBRD, Volume 1* (Budapest–New York: CEU Press), Chapter 12, section 9, p. 339.

26 EBRD Press Release, 22 May 2006. 'EBRD plans major shift in activities to needier regions'.

mention of Turkey as a possible country of operations in the paper, nor in the entire record of the Annual Meeting proceedings. The trail had gone cold.

There were a number of reasons for this development, the most important of which was that the USA was opposed to a change in Turkey's status—the US Director at the EBRD implacably so. Fearful of the consequences of upsetting the USA, Turkey preferred to wait patiently until a consensus looked possible. Although the USA was especially direct in its opposition, this was mainly for ideological reasons rather than as a protest against Turkey per se.

Acting as the tip of a Treasury spear for his colleagues back in Washington (as one American observer put it), the hard-line US Director, Mark Sullivan, firmly pressed the case against Turkey as a country of operations. He was confident in his belief that Turkey was neither a former communist state nor a truly European country, and that legal hurdles would prevent it from becoming a country of operations of the EBRD. The underlying reason for the objection was that the US Treasury was insisting on the EBRD bringing its business to a close. The last thing they wanted was for the Bank to gain a lifeline by opening up business in Turkey since it would spoil the closure agenda.

The idea of a transitory nature for the institution lay in the original negotiations which created the EBRD[27] and was entrenched in the thinking of several key shareholders. Sullivan pushed a long-standing US commitment to the principle of graduation particularly hard and was a leading proponent of the view that the Bank should pay a dividend to shareholders out of profits. This tallied with the "Neocon" agenda pursued by a number of senior administration officials at the time under George W. Bush's presidency. Sullivan, a former Reagan appointee as General Counsel to the US Treasury, was by some accounts close to administration officials who professed little faith in multilateral institutions or the European Union.[28]

The USA had seen the EBRD from the beginning as a different kind of international institution, one that was created for a specific purpose and had a methodology to test when it had reached its goal with the idea that

27 See Kilpatrick, *After the Berlin Wall*, p. 29.

28 An influential advocate of this position was John Bolton, who served in the State department and as US Ambassador to the United Nations during George W. Bush's presidency. Bolton argued that such supranational organisations lacked democratic legitimacy. See for example Stewart M. Patrick, 'John Bolton, Sovereignty Warrior', *Council on Foreign Relations*, 23 March 2018, https://www.cfr.org/blog/john-bolton-sovereignty-warrior.

it would then shut up shop, unlike other UN system institutions some US officials saw as bloated and bureaucratic.

Although less ideological in its perspective, the UK also believed that the EBRD should not have a permanent existence. UK Prime Minister Tony Blair had stressed the point at the EBRD Annual Meeting in 2004, and the Secretary of State for International Development, Hilary Benn, repeated this view in his address as host of the 2006 Meeting: "The Bank was not set up to exist for ever". The view was that the EBRD was a great institution and had done a good job—"we continue to celebrate this [graduation] success story," said Benn. The UK, and especially the USA, saw significant demonstration value from EBRD closure: other international financial institutions (IFIs) would be put on notice that their lifespan was not a given either.

Nonetheless, from a foreign policy perspective Turkey was an important country, especially for the USA given Bush's "freedom agenda" in the Middle East, post-Iraq. Condoleezza Rice, writing of her first trip as US Secretary of State to Ankara in 2005, noted:

> The East and Central Europeans had made a peaceful transition to democracy. Their two lodestars had been NATO and the European Union ... Turkey was a member of NATO but wanted desperately to accede to the European Union. ... But the Europeans were ambivalent in the extreme about integrating more than 70 million Muslims. The Turks felt that Europe was going through the motions of negotiating their entry but unlikely ever to finish the process. Their fears were not unfounded. ... My encounter with the Turkish leaders reinforced my belief that the country could be at the epicenter of a transformed broader Middle East, one that would embrace democratic values ... Prime Minister Recep Tayyip Erdoğan was somewhat harder to read. ... Finally, we established common ground very quickly on the desirability of Turkey's joining the European Union, and I made assurances to intensify the United States' already considerable efforts to make the case to our allies.[29]

The US relationship with Russia was another important factor which influenced US thinking on the EBRD at the time. Some years earlier, welcoming Russian President Vladimir Putin to his Texas ranch at Crawford in the early days of his Presidency, Bush had famously said: "I looked the man

29 Condoleezza Rice, *No Higher Honour* (London: Simon & Schuster), 2011, pp. 330–1.

in the eye. I found him very straightforward and trustworthy—I was able to get a sense of his soul."[30]

By now, in his second term as US President, and after the difficulties encountered (especially at the UN) over the Iraq war, the feeling had soured significantly. The Kremlin had been centralising power: taking over independent television channels, abolishing the election of (regional) governors, prosecuting defiant oligarchs and putting them in prison or into exile. In 2006, Bush was heard to comment: "I think Putin is not a democrat anymore. He's a tsar."[31]

In the EBRD context, these concerns translated into increased US wariness of operations with Russia. As Russia began to move away from market democracy and towards a version of state capitalism, scrutiny of the Bank's activities in Russia intensified. Tensions rose over EBRD financing of Russian oligarchs. Pressure from Russia for increases in Bank investment made things even more difficult for management, and added to US conviction that the time had come to close the EBRD. In US eyes, this was certainly not the time to start expanding into a major economy like Turkey.

For its part, Russia too saw dangers in Turkey becoming a recipient country. Although business in Turkey would likely start small, its GDP was already more than one-half that of Russia and growing fast. Should business volume there replace the Czech Republic, Hungary and Poland for instance, which even as recently as 2004 had absorbed around 14 per cent of the total, Russia's ambitions to see a much greater share would be unlikely to be achieved. The Russian Director, Elena Kotova, raised many questions on the business case for Turkey as a recipient country and its implications for the overall operating framework, including staffing and headroom.[32]

Other countries like the Netherlands, and also the UK, were concerned with the direction the EBRD might take if Turkey became a destination for its investments. They were keen for the Bank to concentrate on poorer and more fragile states in the south and east of the region. Although there

---

30 Bush-Putin Summit, Press Conference, Ljubljana, Slovenia, 16 June 2001, C-Span https://www.c-span.org/video/?c4718091/user-clip-bush-putins-soul. This warmth was not shared by his team who saw more than anything the KGB in his eyes. "Every time Cheney saw Putin, he privately told people, 'I think KGB, KGB, KGB.'" See Peter Baker, 'The Seduction of George W. Bush', *Foreign Policy*, 6 November 2013, https://foreignpolicy.com/2013/11/06/the-seduction-of-george-w-bush/.

31 Baker, 'The Seduction of George W. Bush'.

32 Kotova left the EBRD in 2010 after an investigation into bribery and corruption. Back in Moscow she was charged in 2013 by the Russian interior ministry for soliciting bribes and received a five-year suspended jail sentence.

were areas in eastern Turkey that matched this agenda, the more advanced regions such as Istanbul and its hinterland and sectors such as tourism did not. Turkey was seen as out of line with the EBRD's mission on transition and a distraction from finishing the job it had been asked to do.

The EIB, unlike the European Commission which regarded the EBRD as a valuable source of help in convergence matters, was another EBRD member that voiced objections to EBRD business in Turkey. It made its position clear as early as the 2005 Annual Meeting, where alternate Governor Wolfgang Roth said: "I see no need for ... the EBRD to start becoming active in Turkey, where transition is not the issue at all."

With major shareholders questioning or blocking the way forward, Turkey decided not to press the case but wait. The impasse remained in place for some time given the unchanging positions taken by key shareholders.

However, momentum began to change in 2007 as Turkey became frustrated with the continuing difficulties posed by some shareholders and was emboldened by positive signals coming from the European Commission.

Because of earlier EIB objections and a need to iron out the relationship between the EBRD and EIB in eastern Europe, the southern Caucasus, Russia and Central Asia[33], the Commission had preferred to wait for the dust to settle on the adoption by the EIB of its new external mandate for operations outside EU countries, before pushing Turkey's case.[34] In 2007, they were able to help more concretely.

Meanwhile, Turkey's Alternate Director, Turan Oz, began a diplomatic effort within the EBRD to garner support among those in favour and to see if they could persuade waverers. Elsewhere too, the Turks engaged in a diplomatic push. With the help of the Commission, they succeeded in winning enough support among EU member states for the issue to reach the EU's economic and financial committee in the second half of the year. A discussion at the Economic and Financial Affairs Council (ECOFIN) ministers' lunch on 9 October recognised that a formal view would need to be taken soon, but that first papers on the issue by the Bank could help ministers adopt a position on the matter. The situation had been helped by Philippe Maystadt, the EIB's President, signalling for the first time his openness to discussions with the EBRD over cooperation in Turkey.

33 An MoU covering this region was signed by the EC, EBRD and EIB on 15 December 2006.

34 The mandate covered the period 2007–2013.

3. Management's Response to the Debate

The first formal discussion of Turkey's case took place in October 2007 with a closed session of the Board. There were many questions but two aspects were key: whether and how Turkey could become a recipient country legally, that is in line with the Agreement Establishing the Bank (AEB), and whether it met the political and economic conditions for the Bank to carry out investments in the country.

Legal arguments: principles and interpretation

Management responded to the questions raised by preparing two papers which were discussed at an information session on 23 November. The first paper presented a legal analysis of Turkey as a country of operations.[35] It addressed two aspects of the situation: criteria for being granted recipient status, and how a decision to grant such a status might be made.

The first point for consideration was geography. Under the Agreement, the EBRD was expected to conduct its activities in "Central and Eastern European countries". Despite disagreements elsewhere on whether Turkey was a European country, it was not difficult for the Bank's lawyers to place Turkey in this grouping. In its listing of initial member subscriptions, the Agreement allocated Turkey to the group "Other European countries".[36] Although 95 per cent of Turkey's land mass was in Asia, the paper pointed out that like Russia it was a transcontinental country with a foothold in Europe; and that it was engaged in talks that could eventually lead Turkey to become a member of the EU.

The second issue concerned the transition purpose of the Bank. This posed more of a challenge. The key passage of Article 1 was "to foster the transition towards open-market economies and to promote private and entrepreneurial initiative …". Its origin was the reason that the EBRD was established in the first place, namely the transition of former communist countries towards free markets and democracy. The possibility of a similar 'transition' of a non-communist country like Turkey threw into stark relief

35 EBRD, 'Turkey as a country of operations of the Bank – legal aspects', in 'Legal and Economic Aspects of Turkey as a Country of Operations', 20 November 2007.
36 'Agreement Establishing the European Bank for Reconstruction and Development', Annex A.

the question of whether the EBRD was useful only in its one, original purpose—with its starting-point of socialism and ultimately once completed to become an historical artefact—or whether it might play a similar role beyond its geographical and societal origins.

Turkey would not be the first country to be admitted as a country of operations. Mongolia had been granted this status the previous year and the decision had extended the Bank's geographical remit, though arguably only in a limited way given its border with Russia stretches for more than 2,000 miles. Importantly, however, Mongolia had lived in the shadow of the Soviet Union and as the Mongolian People's Republic it had been governed by its own communist party. Turkey had no communist or socialist antecedents. Indeed, after its founding by Ataturk in 1924 the country had developed first as a secular state and after World War II became a parliamentary republic.

The argument turned on the interpretation of the word "transition" and whether a particular starting condition was necessary for the achievement of the desired end-state. If the world of well-functioning market democracies envisaged in the Articles was the goal, then should it matter what the starting point was provided a country was "committed to and applying the principles of multiparty democracy, pluralism and market economics", as required by Article 1? The size of transition gaps may differ from country to country, but if they were large enough to demand EBRD's attention and the country was striving towards these goals then surely there should be no objection in principle?

Interpretation of meaning can turn on just one or two words, or where they are missing; and it can make a big difference. This was true in the EBRD's case as the absence of the preposition "from" in the Articles was instrumental in its future direction. The paper pointed out,

> The word "transition" is used in several articles of the Agreement to designate the transition of countries to "open market-oriented economies" (Articles 1, 2 & 11). In all these instances, the Agreement describes the state of destination but does not specify the state that precedes it.[37]

And added,

37 Original paper's underlining. 'Agreement Establishing the European Bank for Reconstruction and Development', Annex A, p. 3.

> An ordinary rendering of the word "transition" where it appears in the Agreement Establishing the Bank would permit the Bank's involvement beyond the former communist countries of Europe, in a politically qualifying country of Central and Eastern Europe facing the challenges of the shift to an open market-oriented economy, irrespective of the starting point of that process. On that plain reading, Turkey is eligible to become an additional recipient country.

Other aspects of the Agreement also needed to be considered. Here the interpretation favoured Turkey. Reforms that the Bank was created to support, as detailed in Article 2 of the Agreement Establishing the Bank, such as breaking down state monopolies, decentralisation and the promotion of privatisation were not purely the province of former communist countries but applied equally to Turkey (and other emerging economies).[38]

Turkey shared many of the challenges faced by other transition economies with market gaps most acute in the more remote geographical regions that had not benefitted from economic integration. Despite never having been run by a communist administration, it had, like the eastern European economies, a legacy of widespread state interference.

Turkey's history of strong state control and intervention, trade protection and widespread use of subsidies and significant role of the military in the economy indicated the extent to which reforms were needed. Like many state-dominated economies it needed to sustain and deepen markets and align its institutions more closely with successful open market economies. This after all was one purpose of working towards EU accession. Moreover, the EBRD's mandate to develop the private sector matched well with the Turkish authorities' economic objectives at the time.

The paper argued that while the collapse of communism in eastern Europe was "clearly the spur" to the creation of the EBRD, it did not necessarily preclude other possibilities.

> Arguably, the founders of the Bank may have intended to limit the Bank ... [to] the former "Eastern bloc" ... However, it is also true that ... the

38 In particular, to fulfil the EBRD's purpose, Article 2 required the Bank to assist "recipient member countries to implement structural and sectoral economic reforms, including demonopolization, decentralization and privatization". These aspects had clear relevance to Turkey.

> framers of the Agreement … may have intended not to preclude a different reading … [one which] would permit the Bank to be involved in any Central and Eastern European country facing the challenges of a shift to an open market-oriented economy, although not necessarily from a command economy. This reading would make Turkey, and Turkey only, eligible to become an additional recipient country.[39]

In effect, this shifted the constraint on any expansion of the EBRD to geography rather than history. Countries still had to be committed to and applying principles of democracy and transitioning towards market economies, but the origin of the state and its nexus was no longer a critical defining factor. This was in many ways a decisive change.

Legal arguments: decision methods

Having established that Turkey could legally become a country of operations, the next question was how such a decision might be made. In Mongolia's case, this had involved an amendment of the Agreement and had involved a protracted process requiring acceptance by all members. Given the parlous state of relations between the EBRD and Uzbekistan following the 2003 Annual Meeting in Tashkent, a repeat of the earlier difficulties in obtaining Uzbek consent was all too likely. Fortunately, there was another option under the Articles which entailed the possibility of an interpretation rather than amendment.[40]

The advantage of an interpretation of the Articles was that it did not require unanimity. Given a quorum,[41] Directors could make a decision with not less than two-thirds of the total voting power of members voting. Should any Director request it, the decision could be referred to the Board of Governors. In turn, given a quorum,[42] a decision by Governors required only a majority of the voting power of those voting.

There was nevertheless some uncertainty over whether a decision should be made by amendment or interpretation. There had, however, been a

39 'Agreement Establishing the European Bank for Reconstruction and Development', Annex A, pp. 3–4.

40 Under Article 57 of the Agreement and relevant rules of public international law, in particular Articles 31 and 32 of the 1969 Vienna Convention.

41 In this case, a majority of Directors representing not less than two-thirds of total voting power.

42 For a valid decision this required two-thirds of Governors representing not less than two-thirds of total voting power.

precedent after the dissolution of the Union of Soviet Socialist Republics (USSR) when an interpretative decision was made to lift restrictions on investment under Article 8.4.[43] Directors had granted Japan's request at the time that the decision be referred to Governors. With this in mind, the General Counsel suggested Directors err on the side of caution and follow this route, but with a higher majority requirement: not less than two-thirds of Governors representing not less than three-quarters of the total voting power.

The higher threshold was chosen as it matched the requirement for membership and was thus an upper bound. The great majority of recipient countries had been subject to this test as the Soviet Union and Yugoslavia broke up and, although Turkey was already a member, it was felt that this threshold would provide a more satisfactory, and safer, basis for a decision.

Economic and political arguments

The second paper prepared by management reviewed Turkey's political and economic situation, making comparisons with the transition economies of central and eastern Europe.

From a political perspective the European Council's view from late 2004 that Turkey fulfilled the Copenhagen political criteria, whose scope broadly matched the political aspects of the Bank's mandate under Article 1, was a strong starting point, as was the decision by the Parliamentary Assembly of the Council of Europe that same year to "graduate" Turkey (a founding member since 1949), by ending its monitoring reports on the country.

In the intervening years some further reforms had been undertaken, including Turkey becoming party to the principal international UN human rights treaties and revising its Law on Political Parties to meet international and European commitments. While the implementation of several legal requirements needed more work, there was no reason to reject Turkey's potential application on Article 1 political grounds.

From the economic perspective too, Turkey was making good progress though with more to do. As noted earlier, the macroeconomic situation had become much more stable and growth was strong. Nonetheless, there were many structural and sectoral gaps still to overcome.

43 See Kilpatrick, *After the Berlin Wall*, Chapter 3, section 10, p. 102.

An analysis by the Bank's economists covering 13 EBRD sector groupings, matched against the three categories used for the assessment of transition gaps,[44] showed Turkey was similar to transition countries still undergoing reform, such as Bulgaria and Romania (and a little ahead of Croatia). "Large" transition gaps were identified for energy efficiency and private equity, and to a lesser extent municipal infrastructure,[45] with most gaps assessed as "medium". Of the 39 measured gaps, only seven were assessed as "small".

The implication of the analysis was that considerable potential existed for the EBRD to support Turkey's economic development in a wide range of industrial and financial sectors and in municipalities and their sub-sectors. Substantial regional differences within Turkey, with the east considerably further behind in terms of development, strengthened the case. Furthermore, Turkey's middle ranking in the World Bank's *Doing Business* index (just below Bulgaria and Romania) added to a picture of a country that could benefit from further support for reform.[46]

No formal conclusions were drawn from the session. But the papers and discussion added substance to the momentum that was already building towards making a decision. Several closed sessions of the Board followed in the new year to see whether a consensus might be reached.

4. Turkey's Application, Kyiv and the Strategic Review

By early 2008, it was well over two years since Turkey had first indicated its interest in becoming a country of operations. In the meantime, Turkey's prospects of accession to the EU had deteriorated.[47] Growth was slowing and economic storm clouds were gathering, making access to EBRD finance

---

44 These were the structure and extent of markets; market institutions and policies; and the market-based behaviour of producers. See Kilpatrick, *After the Berlin Wall,* Chapter 10, section 5, p. 282.

45 Municipal and Environmental Infrastructure, which comprised several sub-categories such as water and wastewater services, urban transport, etc., showed a "large" overall gap under market institutions and policies. The quality of services varied between types of infrastructure and across the regions of Turkey, being less well- developed further east.

46 Turkey was ranked 57th (out of 178) in the 2008 *Doing Business* Survey, scoring well on enforcing contracts (34th) and starting a business (43rd), but poorly on dealing with licences (128th) and closing a business (112nd). Bulgaria and Romania were ranked 46th and 48th, respectively, in the *Doing Business* index.

47 The Commission had already published a critical report on Turkey's progress in November 2006, after which negotiations proceeded only slowly and with difficulty. In its Annual Progress Report on Candidate Countries, published in November 2007, the European Commission further highlighted the need for progress on civil liberties, including freedom of expression and religion.

and expertise increasingly attractive. A decision at the EBRD Annual Meeting in Kyiv seemed ideal from Turkey's point of view.

The USA remained unconvinced and continued to hold out against supporting a change in Turkey's status. Turkey remained keen to obtain US agreement and so refrained once more from making its formal request. Its diplomatic push was however beginning to pay dividends. The idea was reaching higher political levels and beyond the confines of finance ministries. In particular, foreign affairs departments and political decision-makers were now considering the proposal.

In the EU, preparations were being made for finance ministers to agree to support Turkey's bid at the next ECOFIN meeting due on 4 March. A consensus had been forged at the ECOFIN lunch a month earlier, on 12 February, where the EIB was no longer objecting and work by the Slovenian presidency along with Turkish diplomatic efforts—demonstrating the political importance they attached to the decision—had persuaded of some of the doubters. Notably, the UK, one of the USA's closest allies and long sceptical of the plan, was ready to change tack and support Turkey. They and other EU finance ministers duly did so at the March meeting.

With the EU on board, their majority shareholding meant that Turkey was in a strong position to push forward. This would not be enough on its own but a US vote against, should it come to it, would not be decisive.[48] It appeared to be over, bar the shouting. Yet the shouting continued.

As late as mid-April, the shareholder split over Turkey appeared to be as wide as ever. A *Wall Street Journal* article quoted Lemierre as saying in an interview that the EU was on the "pro" side with the Americans still opposed:

> Mr. Lemierre said EBRD shareholders have yet to decide whether to invest in Turkey. He said European Union governments are keen to see the bank invest in Turkey, which is in talks to join the bloc. But he said the US opposes such a move, which would be an extension of the bank's original mandate.[49]

---

48 The US shareholding in the EBRD was 10 per cent and with, say, the support of another major non-EU country, such as Japan (with 8.5 per cent), it would still be less than the 25 per cent needed for a blocking minority in this case. Even adding in Russia (4 per cent) would be insufficient.

49 Lemierre, in interview with *The Wall Street Journal*, 17 April 2008.

Turkey's formal application

It was against this backdrop of continuing divergent views about the future of the EBRD that Turkey finally applied for recipient status. The formal application from Turkish Governor İbrahim Çanakçi arrived at the Bank on 24 April. As an official request it would need a response from the Bank one way or another before long. The Turkish authorities, and several of their supporters, hoped a decision could be made in Kyiv at the Annual Meeting the following month (putting some pressure on the Americans), though with only three weeks to go before the meeting this was pushing the bounds of probability.

The letter did not seek to explain in any detail the reasons for Turkey's application but emphasised that the change to Turkey's status "could be done through a decision of the Board of Governors", that is through the interpretative route. Noting the EBRD's ability to contribute to many sectors, Çanakçi wrote, accurately as it turned out, "we believe that changing the status of Turkey in the EBRD will be immensely beneficial for the Bank as well as for Turkey".

The Bank still had to explain how adding Turkey to the list of countries of operations would be managed within the operational financial envelope that had been agreed two years earlier. Again, EBRD management had to perform a delicate balancing act. On the one hand, the Turkish authorities expected becoming a recipient member would be worthwhile financially with a large and rapid build-up of operations to fulfil their and Turkish business expectations. On the other hand, existing countries of operations were wary of any sharing of their claims on Bank resources.[50]

A clarification was sent to the Board towards the end of April, following another closed session of the Board at which a number of questions were raised on how the strategic operating framework parameters might be affected. Management's short answer was that the strategic objectives of the Bank would be unchanged. The only significant change of note, depending on what planning exchange rate assumption was chosen, would be perhaps a small downward adjustment of the strategic reserve in 2010 (the end of the planning period).

The result had been achieved by assuming a "gradual ramp-up" in business volume in Turkey, from no commitments in 2008 (as there was

50 This was especially true of the Russians who, as noted earlier, were already complaining of insufficient attention from the Bank.

insufficient start-up time) to €150 million in 2009 and €300 million in 2010, and that these commitments would be additional to previously agreed overall projected volumes.

Neither Turkey nor the USA found this very satisfactory. The Turkish authorities were disappointed that the business projections were so low, echoing Babacan's initial response three years earlier. The American perspective was different. Their complaint was not simply over figures but with the whole exercise. They were particularly aggrieved by a request from the Bank for a final legal view by 1 May, in time for an executive session just ahead of the Annual Meeting.

This time David McCormick, the US Treasury Undersecretary for International Affairs, after being briefed by the US Director,[51] wrote an excoriating letter to the EBRD President stating not only that his lawyers continued to have "significant reservations" with the Bank's legal interpretation but also that the Bank's analysis had been "woefully inadequate" for such a major decision, including the latest resource assessment. To back up its position, the USA lobbied G7 deputies for a delay in any decision until new EBRD leadership was installed (Lemierre's Presidency was due to end that summer), which deputies agreed in order to placate the USA and reach a consensus on the matter.

McCormick thus proposed a "strategic review" of how Turkey's request fitted the Bank's "broader mandate" to allow a "careful consideration" of Turkey's change of status for a decision to be made "before the end of this year". Despite the forceful tone of the letter, it left some room for manoeuvre by stating that the USA was prepared to play a "constructive role" in the process and would "respect the outcome of any vote at the end of the review".

Given the general view that a consensus, if it could be found, would be the best result, the way forward was now clear. A Strategic Review would be conducted over the coming months and a deadline set for the Board to decide and make a recommendation to Governors on Turkey's request.

The 2008 Annual Meeting

At the 2008 EBRD Annual Meeting in Kyiv, Governors were thus asked to approve a resolution whereby they would request Directors to undertake a

51 The US Director, Mark Sullivan, left the EBRD abruptly soon after Turkey's formal application.

strategic review of the implications of granting recipient country status to Turkey, as part of a process that would see a recommendation going back to Governors by the end of September and a final decision before the end of October.[52]

The Governors adopted the resolution, effectively signalling Turkey's request was almost certainly on track for a positive response. Conference speeches generally expressed strong and warm support for the step now that consensus on this point had been reached. A large number of Governors' statements endorsed Turkey's application with some commenting that they would have preferred to have decided the issue finally at the Kyiv meeting; on the other side, there was simply agreement to the process and review.

Turkey's Governor now explained why Turkey had decided to apply for operational country status. The country wanted to benefit from the EBRD's finance, as well as the expertise in promoting the private sector it had built over more than a decade and a half in central and eastern Europe. Çanakçi said that EBRD support would contribute to Turkey's efforts to speed up privatisation, strengthen the standards of corporate culture and governance, decrease regional disparities, and accelerate the accession process to the EU.

It had been a tricky journey, as a conference speech by Austrian Governor Wilhelm Molterer made clear. Molterer welcomed the move to embrace Turkey, but pointed out that the Turkey question and several other key strategic issues for the EBRD had proven to be divisive, telling delegates: "The rifts which have recently frequently emerged among the Bank's shareholders on the issue of the Bank's future and the commencement of operations in Turkey, as well as on the question of dividends, will have to be healed again."

The UK and USA welcomed the fact that a process been agreed to determine whether and how Turkey could change its status. The head of the UK delegation, Gavin McGillivray, referred to our "our good friend Turkey" and said: "We support the review process to work out how the Bank could make the most effective and appropriate contribution in this important country".

The USA had been particularly keen to place the deliberations over Turkey within the context of a wider review of the EBRD's activities and this they had achieved. McCormick said: "We will work with other shareholders to give Turkey's application a serious and thorough review in the coming months". He stressed the need for a wide-ranging discussion: "Discussion of

52 Resolution No. 113, 'Request by Turkey to become a country of operations', 19 May 2008.

the EBRD's geographical scope and mandate go to the core of the institution and these issues should be considered in an open and transparent way that involves all shareholders."

In a letter to *The Wall Street Journal* published just after Kyiv, McCormick wrote that an editorial by the same newspaper "raises important questions about the possibility of expanding the mandate of the ... EBRD but fails to acknowledge the role of the United States" in establishing a comprehensive and rigorous review for answering them.

Lemierre, in his last appearance as President at an EBRD Annual Meeting, emphasised the benefits to both Turkey and the EBRD of a positive response and was at pains to stress this was the last opportunity for EBRD expansion: "This (change of status) would, of course, support Turkey in developing its private sector, applying the proven EBRD model in the only remaining country in the Bank's geographical scope of Europe."

The Norwegian delegate was even more specific: "Norway can support Turkey's request as a special case, but we are not prepared to accept a further widening of the Bank's geographical mandate."

The Turkish authorities were buoyant at the end of the Kyiv talks. Çanakçi said: "We now strongly expect the management to complete all the necessary work by September and the successful conclusion of our application through a Board of Governors decision by the end of October."

He made clear that the benefits to the EBRD itself were not lost on Turkey: "From the Bank's standpoint, having Turkey as country of operations will certainly contribute to the EBRD's efforts to continue to expand its business volume, to diversify its portfolio, to overcome the existing overconcentration problem, and thus to enrich the Bank's operations."

Strategic Review

Management's strategic review reported to Directors in September. There were no new arguments to those advanced earlier on the legality of the change and the economic challenges Turkey faced ahead. It concentrated largely on the EBRD's objectives in Turkey and that initial business would be small and would not detract from the Bank's efforts in other countries of operations. Concerns with overlaps with other institutions, particularly the EIB and IFC, were dismissed on the grounds of the size of the country and the scale of its needs. The Bank emphasised its active approach to equity

financing, agile responsiveness and client focus and the sectoral expertise it had built over many years in similar market environments.

With agreement on these points, the EBRD's Board of Directors voted on 23 September to recommend that Governors accept Turkey as a recipient. The Governors themselves agreed by late October, voting unanimously in favour of the resolution.[53]

5. Turkey as a Country of Operations

Reflections on the process

Before Turkey expressed an interest in becoming a country of operations, the EBRD's mandate was perfectly clear. At some stage the Bank would close its doors. What was of particular importance at the time of this discussion was the relationship between Turkey and the EU and the EBRD's undoubted successes in supporting the process of EU enlargement. Many Europeans, including the UK, were in favour of Turkey becoming a member of the EU.

It was clear to Lemierre that the usefulness of the Bank was to help to replicate the success of central Europe in Turkey. "Moving to Turkey was not to open the door to a wider base, but mainly to be part of the enlargement process," Lemierre said later. Its geographic proximity fitted this logic and accession set a clear limit.

Lemierre believed those who stressed the importance of Turkey becoming a recipient country in terms of compensating for central and eastern European graduation plans oversimplified the position. In any case, these arguments became academic once it was clear that as a result of the global financial crisis, no country other than the Czech Republic (which had just graduated)[54] left the ambit of the EBRD. Turkey could however help deliver a short-term rebalancing of the portfolio. But also important was the possibility of using profits to increase investments, including support for Turkey's convergence efforts, rather than allocate them to dividend payments.

53 Resolution No. 116. 99.80 per cent of voting power (62 votes) were in favour, as Uzbekistan failed to indicate its position by the deadline.

54 See Kilpatrick, *After the Berlin Wall,* p. 351

As far as the USA was concerned, Lemierre opined, the main factor in favour of swinging behind Turkey's application was its support for a fellow member of the North Atlantic Treaty Organization (NATO). Other commentators, agreeing, linked the final decision by the USA not to stand in the way of the Turkish application to the support, especially within the State Department, for NATO ally Turkey's EU aspirations. Observers understood the US Treasury's espousal of the "sunset bank" view of the EBRD, but also pointed to the State Department, headed during this period by Rice, which looked more at the strategic relationship with Turkey, including the fact this was a NATO member seeking support from an organisation in which the USA was the largest shareholder.

One separate, less public strand, came from Japan and South Korea, countries that had mostly sided with the non-Europeans on strategic issues. The Koreans had just witnessed the EBRD going into Mongolia and had a longer-term vision that, at some time in the future, North Korea could also be on the menu. A Board member involved in the discussions at the time said: "This was definitely a factor for the South Koreans and … indirectly for Japan and indirectly also for the Australians because they shared a chair with the Koreans. So, in this way the Koreans also contributed to bringing the Australians on board."

Once the Japanese authorities had come around, the USA also modified their position. "And then all that counted for them was that they make a clear stand, expressing their views," but no longer standing in the way of a development that had become inevitable.

A key factor for all member countries was the important role played by the diplomacy of Turkey itself. Directors remember still today the very effective campaigning by the Turkish Alternate EBRD Director and Babacan, by then Minister of Foreign Affairs, and the embassies that were active in every capital.

It is important not to underestimate how the decision was seen by the Turkish authorities. Being accepted by the EBRD was a symbolic step on the road to Europe and supported their goals for reform, higher investment and regional integration.

While Turkey saw itself as distinct from central and south-eastern Europe, with its sizeable and experienced private sector, it: "had full confidence that [a] partnership with the EBRD would support Turkey's economic development to the next level, by attracting domestic and

international investment".[55] The Bank's wide range of financial instruments, especially non-sovereign loans and equity, its knowledge of liberalisation, corporate governance and high-quality technical expertise, plus the private sector's familiarity with the EBRD, were further reasons behind the decision.

But, as the Ministry of Treasury and Finance further explained in a retrospective assessment:

> Another major motivation was Turkey's EU accession process. [The] EBRD had helped many countries during their EU accession process … Turkey's accession to EU already had a long history and Turkey was then implementing an ambitious economic reform program to achieve a more open and competitive economy with the prospect of EU accession …
> We felt that being a country of operation of [the] EBRD would contribute to Turkey's economic development and further integration of trade and business relations with Europe and neighbouring countries …
> Our view was that [the] EBRD's support to urban infrastructure, environmental and municipal projects would certainly contribute to our EU accession process.[56]

At the time, perhaps less so a decade later, said one observer, "Turkey wanted to become a European country". It was this that was behind the very persuasive diplomatic activity on the part of the Turkish leadership. When it came to a choice between shareholders holding on to individual policy positions and personal diplomacy, "it was personal diplomacy that won", another commentator said.

The tensions over Turkey highlighted once again the nature of the Bank as a compromise that had been forged from the beginning between the US and continental European perspectives. Turkey had been a tussle between ideological goals on the one hand and the value of integration, economic development and stability in the European neighbourhood on the other.

In the end, shareholders recognised the geopolitical advantages of supporting Turkey, whose authorities had come around to the view that the specific skillset of the EBRD could help their businesses and economic

55 Information from Turkey's Ministry of Treasury and Finance.
56 Information from Turkey's Ministry of Treasury and Finance.

performance. For the EBRD, it seemed the beginning of a beautiful friendship. For Lemierre, in his last significant act as EBRD President, it was a reward for careful preparation and a victory for common sense.

Largest country of operations

On 28 October, the Bank issued an official statement confirming the change in status and announcing the EBRD's investment priorities for Turkey. The Bank said it would focus on five main areas: micro- and small- and medium-sized enterprises by increasing the availability of risk capital and long-term financing, especially outside the main cities; agribusiness, with investments along the food chain; municipal environmental services, through supporting reform and securing efficient delivery of key services, via non-sovereign lending; energy and energy efficiency, by enhancing market conditions and promoting good use of scarce resources; and privatisation in supporting the country's reform programme, through equity finance and expertise.

"A dynamic market economy in Turkey will benefit not only the people of Turkey but also help strengthen other economies in the EBRD region given the country's economic importance," the new EBRD President, Thomas Mirow, said in the statement. "Such a move to help secure a sustainable economic future for the countries in our region is all the more important now at this time of global economic uncertainty."[57]

His comments came less than a month after the collapse of the US investment bank Lehman Brothers—the trigger that unleashed the full force of the global financial crisis that was to have a devastating impact on the EBRD's regions.

Mirow was quick to stress that the move into Turkey would not be replicated. "There is a broad understanding that Turkey is a special case, not a precedent," Mirow said. "It is not a move that should lead to further moves."[58] Mirow also sounded a typically cautious note about the pace of investment in Turkey. Investments would start slowly. "We would have reasons for concern if we were bound to make a huge step," he said. "This is not what we're intending. We want to start modestly."[59]

57 EBRD Press Release, 28 October 2008. 'Turkey to receive EBRD investments of $600 million by 2010'.

58 Paul Hannon, 'EBRD Shareholders Give Go-Ahead For Investment in Turkey', *Dow Jones Newswires*, 28 October 2008.

59 Hannon, 'EBRD Shareholders Give Go-Ahead'.

It was Mike Davey, an experienced EBRD banker from New Zealand, who took over direct responsibility for delivering the EBRD's mandate in the uncharted Turkish waters. Davey was a perfect example of "homo-EBRD" pre-Turkey. He had spent decades in the former Soviet Union and led the EBRD's operations in Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, the Kyrgyz Republic, Moldova, and Tajikistan. In 2009, he moved from Tbilisi to Istanbul as director of the EBRD's newest country of operations, the very personification of the Bank's shift away from the post-communist world of eastern Europe into new territories.

Reflecting on his first impressions a decade later, he highlighted the differences between the former Soviet Union and Turkey—as well as the similarities that made clear the EBRD had a role to play in this new space. Unlike the former Soviet Union, Turkey had a confident business sector, a plethora of big family-owned businesses, a deeper middle class and a vibrant private banking sector. It was, nevertheless, a country in transition, moving away from monolithic business structures. Its economy was opening up and experiencing a return of capital and expertise from the Turkish diaspora. The time was ripe for the EBRD to engage and to apply its experience in pushing forward and developing even further the Turkish spirit of private enterprise.

The niche role for the EBRD among other IFIs active in Turkey was to make a real difference in the private sector—and especially away from major cities such as Istanbul and Ankara. The EBRD could help develop the economically underserved southern and eastern parts of Turkey, promoting small- and medium-sized enterprises that had the best chance of generating jobs in regions of high unemployment. It turned out that the Bank's expertise in working with financial institutions was especially valuable in helping Turkish banks extend loans to these types of companies in less advanced regions and to women entrepreneurs, as well as in other areas such as energy efficiency.

According to Davey, the EBRD helped deliver systemic change in Turkey that went beyond its successful investments across many sectors of the economy. Perhaps its biggest impact was in developing the role of women in the world of Turkish business and in the roll-out of sustainable energy projects.

"As far as the role of women in the economy is concerned, Turkey was challenged. We got involved with gender financing programmes through

the Women in Business programmes and we made a difference."[60] And, on green energy: "We started financing projects in this sector when it was very difficult to invest in renewable energy in Turkey." The Bank's very first project was financing for the country's largest windfarm.[61]

Davey was not surprised by the speed with which the EBRD established itself in Turkey and the pace of its investment growth. There was immediate and very strong demand for the EBRD's finance that outstripped what he was allowed to deliver under early constraints imposed on his team. In the first year of business, investments came in exactly at the €150 million that management had proposed once the go-ahead to do business in Turkey was given.

"At the beginning, we rationed our delivery of projects. But once we had overcome initial caution on the part of some shareholders, we were able to grow much more quickly. The people in Turkey wanted more from us," Davey said. The EBRD was helped by the fact that it was already very well-known in the country, as a result of having been a shareholder since 1991 and because Turkish companies had for many years been active investors with the Bank across its traditional regions.

After the first investment in the windfarm, further financing came thick and fast. Already by 2010, investment volume exceeded the self-imposed cap of €300 million, coming in at just under €500 million. That then doubled to over €1 billion in 2012.

By 2014, when the EBRD stopped funding new investments in Russia in line with shareholder guidance following the annexation of Crimea, Turkey became the EBRD's largest country of operations by annual business volume. Just one year later, with annual investment approaching €2 billion, the EBRD's biggest country investment portfolio was in Turkey at just under €6 billion.

Turkey had indeed stepped in to fill a revenue gap the EBRD was facing that would become more significant after 2008, but not in quite the way shareholders, or management, had anticipated. The financing gap had not materialised from central and eastern Europe. As the global financial crisis intensified, the graduation of the EU-8 for all but the Czech Republic was

60 Interview, January 2021.

61 In March 2009, the Board approved a project with Rotor Windfarm, a 54 turbine (135 MW) onshore windfarm in Osmaniye, involving €45 million financing by the EBRD to a company owned by Zorlu Energji, part of Zorlu Holding, a large Turkish conglomerate.

put on ice. The crisis led to a sharp increase in demand for EBRD financing. On the other hand, the subsequent fall away from Russia was abrupt.

Nor did the EU vision that informed the EBRD's early aims for Turkey at the very start of the negotiations turn out to be the real driver of the relationship in the end. EU membership had become nothing more than a distant hope by 2018 when a European Council meeting put a clear block on further accession negotiations:

> The Council notes that Turkey has been moving further away from the European Union. Turkey's accession negotiations have therefore effectively come to a standstill and no further chapters can be considered for opening or closing and no further work towards the modernisation of the EU–Turkey Customs Union is foreseen.[62]

Yet the gamble had paid off. The EBRD was helping to bring about systemic change and economic progress in Turkey by making and encouraging substantial investments, almost exclusively in the private sector. At the same time, Turkey was contributing to the EBRD's ability to scale up development support at a time of crisis.

From the Turkish perspective, there was appreciation too for what was achieved as a result of the strengthened relationship.[63] Turkey's new status "came at a time ... when international support was seen as an assurance for ... the stability of national economies", while "Turkish companies benefitted from EBRD's experience, know-how transfers and strong technical capacity".

In the judgement of the Ministry of Treasury and Finance, "EBRD's open and flexible business model [means] that the EBRD is perceived as one [of] the most efficient international financial institutions in addressing obstacles in business ... [and] a preferred development partner". "Non-sovereign loans to municipalities and private sector", its "contribution to the privatisation process"[64] and "help in introducing new PPP schemes" were all

62 EU Press release. 'Enlargement and Stabilisation and Association Process – Council conclusions,' https://www.consilium.europa.eu/media/35863/st10555-en18.pdf.

63 Information from Turkey's Ministry of Treasury and Finance.

64 The EBRD has been involved in seven privatisation projects in Turkey, mainly in the transportation, energy and agribusiness sectors for a total amount of more than US$ 500 million. Source: Turkey's Ministry of Treasury and Finance.

attractive dimensions of the institution. A focus on the renewable energy sector—three-quarters of Turkey's energy demand is imported—was also cited as a prominent area of cooperation: "EBRD has contributed to reduce Turkey's energy dependence and also the chronic current account deficit".

After almost €13 billion of financing for projects since Turkey became a country of operations, the Ministry noted that the EBRD is: "Turkey's second largest development partner among all MDBs [and that] 96% of EBRD's lending to Turkey has been to the private sector".[65]

As was stressed repeatedly during the Turkey negotiations, this expansion was supposed to be the last, the exception to the rule that the EBRD was a transition bank with a finite mandate. However, the remarks of the Egyptian delegate to the 2008 Annual Meeting in Kyiv seemed eerily prescient just three years later when the EBRD was being called upon to join in the international response to the economic challenges of the Arab Spring. Egyptian Governor Fayza Aboulnaga told the Kyiv conference, "Egypt supports Turkey's change of status to that of a country of operations and we are pleased to see consensus emerging on this issue. This is a positive precedent."

Within seven years Turkey and other south-eastern Mediterranean countries would provide the bulk of EBRD business activity, and two years later the majority of its portfolio. The corridor of investments that once stretched from Warsaw to Moscow, and which defined the first period of the EBRD's existence, now pointed towards Istanbul and beyond. It had been a stressful and bumpy journey, but the pivot to Turkey was just the first step that changed the Bank for ever.

65 Ministry of Treasury and Finance, ibid.

Chapter 2

Markets in Crisis

Introduction

By 2007, the economies of the EBRD region were growing at a record pace. The region was basking in the success of a sustained period of economic improvement. Many countries had embraced democracy and the principles of the market economy. Eight of the countries where the EBRD was investing were now established EU member states and preparing to leave the ambit of the Bank. Two more had joined the EU at the start of the year. Naturally, many delegates at its annual meeting in Kazan in May congratulated the EBRD on a job that was progressing well.

In the previous four years, GDP growth in the region had accelerated to a rate of almost 7 per cent a year, up from an already high rate of around 5 per cent a year between 2000 and 2003. Even more striking was the breadth of improvement that had taken place. Each of the 30 EBRD countries of operations had seen increases in output for seven years in a row (other than a 0.2 per cent fall in Kyrgyz Republic in 2005). The region's GDP was now more than 50 per cent above its level at the start of the millennium.

Income convergence with western economies was finally happening across the board, especially for those closest to or within the EU.

This rosy economic picture was no less true for some of the Soviet Union's former republics. In the Baltic states, growth had accelerated to 10 per cent a year by 2007. Many resource-rich countries in the Caucasus and Central Asia had seen increases in GDP that were nothing less than spectacular, helped by the acceleration in commodity prices. In Armenia, Azerbaijan, Kazakhstan and Turkmenistan, GDP had more than doubled since 2000. Households were beginning to see the fruits of these developments.

For the Kazakh farmer, just as for his counterpart in the US Midwest, improvements were unmistakable. Wheat prices and incomes were rising, banks were keen to lend for business expansion and real estate values were booming. Working on opposite sides of the world, twelve time zones apart, the once ideological enemies were now an integral part of a continuous global production cycle and appeared to share a common future of growth and prosperity.

What they shared in fact was a common underlying and serious problem: a rampant financial sector with little respect for borrowers' ability to repay. In a matter of months their dreams would be shattered, and with them those of many more, as a financial tornado tore through the USA and Kazakhstan before morphing into a global financial crisis.

1. Financial Problems in Kazakhstan

Kazakhstan was indeed an early outlier in the crisis that was to engulf the whole of the EBRD region and a harbinger of what was to come more widely.

An attractive investment opportunity

A plentiful supply of oil and gas, mineral resources and a vast, highly-fertile agricultural landscape—covering an area the size of western Europe—had allowed Kazakhstan to tap international capital markets as interest in emerging economies re-emerged in the 2000s. A period of economic reform after the Russian crisis—efforts which won praise from the IMF—resulted in a strong macroeconomic performance, despite currency appreciation pressures from financial inflows as growth rocketed. At the time, Kazakhstan even earned the epithet of 'tiger of the steppe' in a comparison—wholly misplaced in retrospect—to fast-growing Asian economies such as South Korea and Taiwan. Unlike Kazakhstan, these original Asian Tigers had built strong manufacturing sectors and had little by way of natural resources.

Rising production and a steep increase in global commodity prices propelled its economy and the net inflow of FDI, already running at almost US$ 3 billion a year in the first half of the decade, grew to around US$ 12 billion by 2007. Foreign exchange earnings grew similarly fast and provided

ready fuel to spur on the financial system to offer new loans to businesses and households who were more than eager to join the spending spree.

As the economy was booming, the country's banks, primarily domestic, had expanded rapidly, competing fiercely for market share at home while also spreading their reach to foreign markets. Investor confidence was high and banks like Bank TuranAlem (later renamed BTA Bank) and Kazkommerzbank (KKB), the largest bank in Kazakhstan, both of which had been early EBRD clients,[1] were easily able to raise funding on the international credit markets.

With a stable exchange rate, the ability to borrow abroad in hard currency at low interest rates and charge double-digit rates in tenge to customers at home became irresistible for Kazakh banks. Ignoring growing balance sheet mismatches and the risk of a sudden depreciation, the banks piled on their exposures as profits rose. Construction and property became the outlet for this growing pool of liquidity and real estate prices accelerated, most noticeably in major cities like Almaty and Astana. In short, Kazakhstan's economy fell victim to a speculative construction and property boom as domestic credit expanded at over 60 per cent a year—even increasing by 80 per cent in 2006.[2]

Investing in the financial sector

André Küüsvek, an Estonian banker who moved to run the EBRD's operations in Kazakhstan in 2004, recalled that around two-thirds of the EBRD's portfolio in the country in those days was in the financial sector. There was little opportunity for involvement in municipal areas and the corporate sector was largely in the hands of oligarchs.

For the EBRD, the model of developing the domestic financial sector as a means of intermediating funds generated by resource sectors, thereby allowing them to be reallocated towards productive, job-creating sectors, especially to SMEs, or for industrial energy efficiency, underpinned this thinking.

1 The EBRD had exposure to BTA through its trade finance and grain receipts' programmes before it purchased convertible preference redeemable shares in BTA in 2001, alongside other IFIs. Following a loan in 1998, the EBRD purchased an equity stake in KKB in 2003. Preference shares in BTA were converted to ordinary shares in 2006.

2 The EBRD *Transition Report*, published in 2007, noted that almost one-half of all bank liabilities originated abroad and that the property sector accounted for more than 32 per cent of bank lending at the end of 2006.

In addition to the credit lines, the EBRD also held equity stakes in KKB and BTA. Both banks were competing for better market share. However, Küüsvek noted that while the largest banks were successfully raising money internationally via large syndications and foreign listings there was in fact little scope to reinvest the scale of these funds effectively back at home. Consequently, much of the financing was funnelled directly into the construction industry, fuelling a property bubble that would soon burst spectacularly.

Awkwardly, there were also clear examples of 'connected banking', where banks conduct their lending on the basis of (sometimes too cosy) relationships with business associates and related companies. The EBRD grew increasingly wary of the activities at BTA, especially after the return to the helm of the bank of its major shareholder, Mukhtar Ablyazov. Ablyazov, who had been freed from jail in 2003[3] and subsequently fled the country (in 2009), was to be accused and convicted of fraud—and, many years later even murder, following the death by shooting of the former co-owner of BTA, Yerzhan Tatishev.

Tatishev died in what was originally billed as a freak hunting accident in 2004, at a time when Ablyazov was no longer at the bank and out of favour with the administration of President Nursultan Nazarbayev. But in 2005, at a hastily called extraordinary shareholders meeting, Ablyazov was brought back into the fold and appointed chairman of BTA's board of directors.

Ablyazov returned with big ideas for the bank. Küüsvek was not convinced. He and the Austrian head of financial institutions at the EBRD, Kurt Geiger, went to see the reinstated head of BTA. The EBRD decided there would be no further transactions with BTA but that it would nonetheless remain a shareholder.[4]

Instead, as the largest foreign investor in Kazakhstan outside the oil and gas sector, the EBRD sought diversification opportunities and shifted its portfolio away from financial institutions towards the corporate and power sectors. It managed to maintain strong growth in its predominantly non-sovereign business volume.[5]

---

3 Ablyazov had been a Minister for Energy, Industry and Trade before helping to found the Democratic Choice of Kazakhstan (DCK) in 2001, a political party that posed a challenge to the Nazarbayev regime. He was jailed for six years for abuse of office and illegal financial dealing in 2002 but, after promising to stay out of politics, was released in 2003. See 'Former managing director of BTA Bank extradited to Kazakhstan from UAE', Fergana News Agency, 5 March 2020, https://en.fergana.news/news/115794/.

4 The EBRD's eventual exit from BTA took place in 2011.

5 In 2007, the non-sovereign share was 88 per cent, with the portfolio increasing by more than one-third in that year alone.

It was against this backdrop of heady financial sector growth, a booming property market and a rapidly expanding economy that things began to turn in 2007.

The turn in 2007

Commercial bank lending had been accelerating over several years, heavily reliant on international wholesale funding and debt securities with bullet repayment structures. Credit risk indicators such as loan-to-deposit ratios (LDRs) had soared to over 150 per cent and in many banks more than one-third of exposure was to construction and real estate (with residential mortgages adding further to the concentration risk).

Concerned at the unsustainable pace of credit growth, the Kazakh regulatory agency, the FSA, imposed a number of measures in the second half of 2006, including limits on banks' short-term external borrowing. Nonetheless, banking assets continued to expand fast, doubling that year, and private external debt jumped to over 90 per cent of GDP.

The FSA deployed a further round of prudential tightening the following April. But by then, bank margins were being squeezed and asset growth had started to slow, even though house prices continued their upward track for a few months more.

The deceleration of credit growth was compounded by the first ripples of the subprime mortgage crisis in the USA. As Bear Stearns, a New York global investment bank, reported mounting losses on subprime exposures in July 2007, international banks started to look more critically at riskier assets. Kazakhstan's onerous external obligations were an obvious source of vulnerability, particularly when set against a domestic boom based on shaky foundations.

The country's copious exposure to foreign finance suddenly turned what had looked like a positive sign of transition and integration with the world of international capital into a major liability, as access to funding dried up amid a widening global credit chill. No longer able to access foreign funding or refinance foreign obligations coming due, Kazakh banks sharply cut back on new lending and began to raise interest rates.

Prior to Bear Stearns, most commentators remained relatively sanguine at the unfolding picture—for example, Moody's noted the low level of government debt, virtually none of which was external, and the build-up of foreign exchange reserves in the National Fund.

By October 2007, however, it was clear that the global rise in investor nervousness and increasing risk aversion on the part of lenders worldwide was now a major threat to the country's economy. On 8 October, Standard & Poor's (S&P) cut its rating for Kazakh debt, citing a significant tightening in credit conditions for borrowers. Announcing the step, S&P analyst Luc Marchand said:

> The rating downgrades reflect funding problems in the Kazakh financial system. [...] Since July, falling domestic depositor confidence and difficulties in rolling over maturing international syndicated loans and cross-border interbank deposits have forced Kazakh banks to obtain short-term funding from the National Bank of Kazakhstan to support their liquidity.[6]

The downgrade was a trigger for furious activity to try to restore calm to the worried markets. Nazarbayev, the country's powerful president, said the government would support the country's commercial banks and instructed the authorities to free up US$ 4 billion to do so. He also criticised the ratings agencies and called the downgrade unfounded, while his Prime Minister Karim Massimov was quoted as complaining that the country was under attack from hedge funds and vowing "we shall fight back".[7]

During a press conference in the northern city of Pavlodar in December, the Kazakh President told reporters:

> I think ratings agencies should think more thoroughly and understand that Kazakhstan stands firmly on its feet and will not allow any Kazakh bank to collapse ... The economy is stable ... It's not objective that the ratings are being cut.[8]

By February 2008, in his annual state of the nation address, Nazarbayev acknowledged that the problems emanating from the USA had indeed become a problem for Kazakhstan and he called on his government to take steps to curb the volatility on the domestic financial sector:

---

6 'Kazakhstan's Sovereign Rating Cut By S&P on Funding Issues', Dow Jones, 8 October 2007.

7 David Litterick, 'Angry Kazakhstan props up bank shares', *The Telegraph,* 13 October 2007, https://www.telegraph.co.uk/finance/markets/2817642/Angry-Kazakhstan-props-up-bank-shares.html.

8 'Kazakh leader says he won't let banks collapse', *Reuters News,* 12 December 2007.

> We must learn lessons stemming from the US mortgage crisis which has had a serious impact on the global financial system as well as our banks. … We have to intensify work to fight inflation. The government must temporarily … cut state spending across the board apart from social spending … This will help ease inflationary pressure.[9]

That same month, Küüsvek announced that the EBRD was planning to earmark up to half a billion dollars in funding for Kazakh banks to help them overcome their problems with borrowing on the international markets:

> We plan to sign new projects worth about US$ 1 billion this year and maybe half of that will be with banks. In the second half (of this year) we might try to reopen the syndicated loan market for Kazakh banks.[10]

The Kazakh authorities responded decisively to the problems faced by the financial sector, pumping in central bank liquidity and creating a financing facility for lending to construction companies and small firms. But external forces became too strong for this medicine to have its desired effect.

Any optimism about an early recovery from the problems in the economy was short-lived once the full force of the global crisis became apparent in the wake of the collapse of US investment bank Lehman Brothers in September 2008. Kazakhstan was now confronting a 'double whammy' from its dependence on foreign borrowing and commodity exports, and its banks were in the front line.

By November, Finance Minister Bolat Zhamishev was saying that Kazakhstan once again faced "huge risks" following a precipitous fall in the oil price.[11] He noted:

> Now that a second wave of the crisis has engulfed us, we have to realise that a period of rapid economic growth due to high oil prices (has ended) … we have to ensure the economy evolves … with the smallest possible losses.[12]

---

9 'Kazakh leader urges less spending, more exploration', *Reuters News*, 6 February 2008.

10 Olzhas Auyezov, 'EBRD to support Kazakh banks amid credit woes', *Reuters*, 19 February 2008, https://www.reuters.com/article/rbssFinancialServicesAndRealEstateNews/idUSL1989648720080219.

11 Oil prices (WTI) fell from around US$ 140 per barrel at their peak in June 2008 to US$ 50 per barrel in November, reaching a low of US$ 45 per barrel at the turn of the year.

12 Mark Thompson and Maria Golovnina, 'Kazakhstan faces "huge risks" – finance minister', *Reuters News*, 21 November 2008.

Bank debt was also a big concern with non-performing loans rising rapidly following the collapse in house prices which triggered insolvencies in the construction sector.[13]

As the crisis unfolded into 2009, the Kazakh government pitched in to buy up shares in the biggest banks: BTA, in which it bought new shares representing three-quarters of the stock, KKB and Halyk.[14] Already having seen a drop in GDP growth of 7 percentage points in 2008 against the average for the decade,[15] Kazakhstan's economy was now facing a highly uncertain future.

2. Contagion and Crisis

From Kazakhstan to Europe

Kazakhstan's boom on the back of huge flows of foreign bank finance had been extreme. Primarily driven by emerging markets investors' desire to exploit a growing economy with large supplies of natural resources, the financial flows had enabled domestic expansion. But as oil prices plunged, a significant devaluation of tenge followed in February 2009. The currency mismatches on the balance sheets of the Kazakh banks came back to haunt them. What had been an early casualty of imprudent financial behaviour became a full-blown crisis, and significant bank rescue efforts followed.

Further west it was not natural resources that had enticed foreign banks to follow a similar path into the EBRD region but skills, low wages and proximity to the large market of the European Union. The economic boom here had been more broadly based and, for most countries, more measured. But it exhibited the same dynamic of foreign finance leading the way and encouraging large-scale bank borrowing, mostly in foreign currencies.

Foreign banks dominated the region's banking systems. In some cases, such as Estonia, it was virtually total—99 per cent of banking assets were foreign-owned—but even for central and south-eastern Europe, foreign

---

13 The house price index fell by around one-fifth between the summer 2007 peak and October and dropped by a further one-third by the end of 2008, meaning average prices had more or less halved in eighteen months. *Source*: Trading Economics.

14 EBRD *Transition Report 2009*, p. 176.

15 GDP growth fell to 3.3 per cent in 2008 from an average of 10.1 per cent since the turn of the decade, and dropped to 1.2 per cent in 2009. Growth in per capita GDP turned negative.

bank penetration was some 80 per cent in 2006 and rising. It is no surprise that when the financial crisis hit global banks with hurricane-like force in the autumn of 2008 it was these countries, like Kazakhstan, that were caught severely in its path.

Misplaced optimism

A year earlier it had all looked different. Buoyed by years of solid growth, the emerging economies of former communist eastern Europe appeared more or less impervious to the wave of dire financial news sweeping over the Atlantic. Even as the US sub-prime mortgage crisis metamorphosed into a credit crunch in western Europe, and clouds gathered over eastern Europe, the impact was still expected to be manageable.

That changed in one fell swoop with the bankruptcy of Lehman Brothers on 15 September 2008. Confident assertions about an imminent successful conclusion of the transition journey for many economies in eastern Europe melted away. Growth forecasts were wound back savagely and repeatedly. Eastern Europe ultimately turned out to be the emerging region of the world hardest hit by the crisis.

In retrospect, many saw the Lehman collapse not so much as the cause of the rapid descent of the eastern European economies, but as a catalyst that revealed underlying frailties. As the economic downturn deepened, it became clear that record levels of growth had been masking deep-seated residual challenges in the economies where the EBRD was active.

There was no doubt that the post-communist states had made remarkable progress in terms of wholesale economic transformation. However, the path to economic convergence with the more advanced economies beyond the EBRD region was going to be much longer and more arduous than originally anticipated.

Only four months before the Lehman shock, the EBRD had produced a set of relatively optimistic forecasts that reflected the prevailing view of the region. Growth would moderate slightly across the EBRD's countries as a whole, in line with the global economic climate.

That was not entirely bad news. The previous growth rates were becoming unsustainable, based on inflows of foreign capital that might dry up. The region would still see respectable growth of some 6 per cent for 2008, only a little below the robust rate of 7 per cent recorded in 2007.

In their May 2008 Economic Forecast, the EBRD economists wrote, "The international credit crisis has so far only had a limited impact on the region as whole. Banks in the region had little if any exposure to structured assets linked to US mortgage markets."[16]

The economists warned that any protracted stress on the western financial markets could lead to a sharper than expected downturn in capital flows to the region, exposing the substantial external financing requirements of some countries, especially in the Baltics and south-eastern Europe.[17]

Downturn takes hold

By November, when the EBRD issued its 2008 *Transition Report*, the temperature was markedly different. The pace of growth across the EBRD regions was now expected to drop sharply to 3 per cent in 2009, according to new forecasts, almost half that predicted just six months earlier.

This *Transition Report*, entitled somewhat tenuously by the time of publication "Growth in Transition", recognised the abnormality of the situation. The EBRD Chief Economist Erik Berglof, a Swedish economics professor previously in charge of the Centre for Economic and Financial Research at the New Economic School in Moscow, who had taken over from Willem Buiter in 2006, said:

> There are now increasing signs that the wider economy is being affected, with industrial production slowing down and even contracting in many countries. These developments stem not only from more expensive credit and a rapid reduction of growth in key export markets, but also increasingly from the shutdown of traditional lending channels.[18]

He pointed out that stabilisation of banking systems would need to be the priority for governments across the whole region. Hinting at the intense and productive cross-border cooperation in which he personally would later play a key role, Berglof added,

16 EBRD Press Release, 18 May 2008. 'EBRD sees moderation in 2008 economic growth as the global economy deteriorates'.

17 EBRD Press Release, 18 May 2008. 'EBRD sees moderation in 2008 economic growth as the global economy deteriorates'.

18 'Growth in Transition', EBRD *Transition Report, 2008*, p. vi.

> Stabilisation measures will need to be coordinated with other countries—both in western Europe and in other transition countries—taking account of the inter-linking ownership structures in the region's financial system.[19]

The EBRD's new President, Thomas Mirow, who arrived in office just as the conflict between Russia and Georgia erupted (Chapter 5) was now facing a major economic crisis in the region the EBRD, and he as its President, was charged to support. It was a true baptism of fire.

Mirow was in no doubt about the sort of impact the financial crisis would have on the institution he was leading. He began by telling shareholders that the Bank's profitability was under threat for the first time since the 1998 Russian crisis. The damage included a US$ 135 million exposure to the now bankrupt Lehman itself, which would have to be marked down as an impairment. In October, *The Financial Times* quoted Mirow as saying, "the EBRD will be hit ... To what degree is not yet completely clear ... But we will see write-downs on our listed equities and on the unlisted."[20]

It was too soon to gauge the full extent of the impact that would be wrought across the region by the global financial meltdown, but the direction was clear. As each day passed the outlook appeared increasingly bleak as the "sudden stop" of finance took more and more banks and companies to the brink of collapse.

The EBRD's downgraded economic forecasts turned out to be far too optimistic, like others at the time. The about-turn in the region's output was on an unparalleled scale. Predicted growth went from *plus* 6 per cent in 2008 to *minus* 6 per cent a year later, although the final outturn transpired to be not quite as dramatically bad.

The effect on the EBRD's finances was also pronounced. When they came, the EBRD's losses dwarfed the €61 million shortfall experienced in 1998. After earning profits just shy of €2 billion in 2007, the Bank's account was to swing into losses of €602 million in 2008 and €746 million in 2009.

For Mirow, there was no question that the EBRD had to respond. But how? And what would shareholders be prepared to do to help? These were the questions that needed to be addressed as he prepared the ground for action.

---

19 EBRD Press Release, 25 November 2008. 'EBRD economies to slow sharply in 2009'.

20 Stefan Wagstyl, 'EBRD aces first loss in decade', *Financial Times*, 24 October 2008, https://www.ft.com/content/f53bcb7a-a1ee-11dd-a32f-000077b07658.

3. Preparing a First Response

On 17 and 18 November, Mirow and his team decamped to a hotel in the Hertfordshire countryside with the Board of Directors for a retreat to discuss the EBRD's next steps. It was early days and there was a certain amount of caution among the assembled company.

Management was at pains to make it clear right from the word go what the EBRD could do and—just as importantly—what it could not do. The Bank provided project finance and projects needed preparation, which could take some time. Projects also needed to meet sound banking criteria. The EBRD was not the International Monetary Fund (IMF). It did not have a mandate to manage macroeconomic crises: it did not finance fiscal or balance of payments gaps. Nor was it a lender of last resort.

Nonetheless, it had a duty to support its clients where feasible and a solid track record of helping the authorities to find policy solutions in difficult situations, working alongside other international financial institutions.

Not the IMF but an active market participant

An internal debate about the EBRD's role in response to the crisis had been underway before the retreat. According to Jeromin Zettelmeyer, a former IMF economist then at the EBRD, it was the strict definition of the mandate that engendered the Bank's initial caution as the crisis started to engulf the EBRD's regions. As he later recalled, "the EBRD was not set up to be a crisis fighting institution. Crisis management was for the IMF. The EBRD was about long-term development and transition."

It was not immediately obvious what role the EBRD could play, Zettelmeyer said.[21]

This was certainly correct from a strict macroeconomic perspective. The IMF had long years of experience in dealing with economic crises all around the globe, while the EU had a leading role in policy formulation for many of the EBRD's countries. The EBRD was far smaller than the European Investment Bank (EIB), whose reach by now extended well beyond the boundaries of the EU. The EBRD could not respond alone with the vast amounts of finance that was clearly needed.

21 Interview, 2020.

Although the EBRD lacked the financial firepower to stem the macro effects of the crisis the economists foresaw the outlines of a coordination role in which the EBRD might play a significant part, especially as it was acknowledged to be a major, and often *the* major, investor in the countries of its region.

At a micro level, the Banking Department too could see a way of playing a role and had some experience of dealing with crises, albeit on a much smaller scale than what they were now confronting. After all, the EBRD was a nimble private-sector focused and demand-led institution. Its ear was close to the ground where the crisis was happening, in the periphery of the EU and further afield. Intimate local knowledge distilled from more than fifteen years of working with clients in its countries of operations, and with offices in every country, large and small, was a unique asset.

For their part, the bankers knew that the EBRD's balance sheet had at least some capacity to help well-run companies and banks survive the intense pressures they were under and make it to the other side of the economic cycle. They were already at work with clients on restructurings and devising rescue packages and ready to provide advice to companies, banks and policymakers.

IFI coordination

Berglof was acutely aware of the imbalance between eurozone-led banks and central, eastern, and south-eastern European (CESEE) banking systems and the risks this imposed on the region. Coordination failures were a common feature of international crises and he could see the problems that lay ahead. Fortunately, the OCE team he had built was well-suited to the task of finding a solution.

Zettelmeyer had cut his teeth at the IMF researching debt defaults and complex resolution mechanisms, while his colleague, Piroska Nagy-Mohácsi, a Hungarian economist and another recent IMF recruit, was corralling international institutions to help with the crisis in Georgia that had erupted earlier in 2008, and one of the present authors[22] had experience as a former head of delegation to the Paris Club, an official debt resolution agency. The team quickly reached a view on the strong need for coordination, notably between the public and private sectors.

22 Andrew Kilpatrick.

What had started as a private sector banking problem was rapidly escalating into a public sector one, as cries for help grew and unemployment rose. The EBRD's niche role was its focus on the private sector, whereas the IMF and World Bank dealt with the public sector. "We were uniquely positioned to play a private-public coordination role for which the EBRD was created," said Zettelmeyer. The economists ran with this idea, leading the way with an action plan that just a few months later would become known as the Vienna Initiative.

The group also strongly believed that all of the multilateral development banks (MDBs) together could play a key counter-cyclical role, with each bringing something special to the table. This was seen as especially important for the many countries in the region which lacked the fiscal capacity to offset the recessionary forces now at work.

The prominent role assumed by the economists in those early days of crisis response was something of a novelty, which in some Bank circles was viewed with a certain suspicion. Zettelmeyer recalls: "The EBRD position was complicated by the fact that the initial formulation of the crisis response—the initial thinking about it—was an OCE-led exercise. The Bank was not used to being led by the OCE."

Typically, economists' advice was to warn when to put the brakes on and sound notes of caution about whether projects put forward by bankers really conformed with the mandate and had meaningful impact on the transition process. But, Zettelmeyer said: "The bankers welcomed the OCE initiative, because by leading a coordinated response the EBRD was protecting its investments."

Mirow contemplates what's needed

Although ahead of the game, the economists were aware they had to persuade the new President of the wisdom of pushing a more prominent role for the EBRD, including in terms of increased investment, when the financial world appeared to be in retreat. At that time, the inclination of every commercial bank was to turn inwards and protect assets, reduce risk exposures and withdraw from markets and new business.

As a former State Secretary at the Federal German Finance Ministry—famed for its strict budgetary policy—at first sight Mirow might have appeared an unlikely candidate for such a radical strategy. Significant expansion could also lead to pressure on the EBRD's balance sheet and potentially

to a capital increase, which did not appear to be on the cards, since he had only recently ruled it out during the debate over Turkey.

This was a time of difficult choices. Mirow, whose habit of collecting his thoughts in silence behind closed doors contrasted with his predecessors, nonetheless rapidly concluded there was only one logical route forward. The EBRD needed to be cautious, yes, prudentially as a bank, but it also needed to be bold, demonstrably above the fray as a supranational institution.

The pressures were unprecedented but Mirow saw virtue in leading the charge to redress the financial failures hitting the EBRD region so dramatically hard, and that to do so effectively would require joining with other international actors to strengthen the position. He also surmised that shareholder support would be crucial to the endeavour and this formed part of his thinking ahead of the Hertfordshire retreat.

It was doubly fortunate that Mirow had recently appointed a very able member of staff to head his office, Hans Peter Lankes, an economist who had served as Berglof's previous deputy. Lankes, a fellow German national, was not only familiar with the region but also knew the EBRD inside-out having played a major role in its development (Volume 1, Chapter 10).

Mirow, as a former G7 deputy, was also well-connected to the international financial coordination mechanisms that were getting under way. This followed US action to support its financial institutions and the recapitalisations of British banks, led by a call from UK Prime Minister Gordon Brown for a global rescue effort to prevent a total collapse of the financial system and a recession comparable to the Great Depression of the 1930s.

Armed with the arguments that management had prepared, Mirow presented the case for action at the November retreat of the EBRD Board.

4. Gearing Up

Despite the initial caution of many shareholder representatives present at the retreat, the effect of discussing the issues collectively helped to amplify the view that this was no ordinary downturn and that the situation was particularly perilous for the EBRD region and the fate of its transition. Capitals would need to be carefully briefed on the central and eastern European situation with the hope that they would pay close attention to it, notwithstanding the enormous domestic pressures they were under.

Fresh from the rural retreat, and eager to consolidate the gains made at the meeting, Mirow wrote to shareholders right away outlining the consensus for an EBRD response that had been forged during the discussions in Hertfordshire. There was, said Mirow, clear agreement on the need for a determined EBRD response that would send a clear signal of the Bank's preparedness to support its countries of operations:

> Given the limited resources of the Bank relative to the magnitude of the challenge, the Bank's response must be based on its country and project expertise and not in the first instance on lending volume ... [and] be guided ... by its core operating principles of transition impact, sound banking and additionality.[23]

Significantly, the EBRD would respond to the needs of all countries, including the more advanced economies in central Europe and the Baltics, "without questioning graduation". A crucial element in the response would be a significant reinforcement of coordination with other IFIs "in order to leverage on each other's particular strengths".

Mirow was careful to leave room for higher business volume and proposed to shareholders that investments would rise to €7 billion in 2009—a 20 per cent increase on the upper bound that had been set for 2008.

The €7 billion reflected a mid-scenario that assumed a resolution of the global financial crisis and a resumption of growth by 2010. Given the uncertainties and a "significant likelihood" of a more pessimistic economic scenario, the projections also considered the possibility that the Bank's business volume would be constrained even with a resolute crisis response effort.

The President's proposals, based around the mid-scenario and plans for scaled-up financing, were adopted by the Board on 10 December.

5. EBRD's Early Operational Efforts

The EBRD's initial response was designed to focus especially on supporting the region's banks and making sure finance kept flowing, in particular to small- and medium-sized firms. The broader corporate sector was expected

23 'Letter from the President following the Bank Retreat', EBRD, 19 November 2008.

to benefit from extending working capital lines and short-term debt refinancing, while the EBRD's Trade Facilitation Programme (TFP), which was a well-established product valued highly by clients, was expanded, keeping trade flowing to and from the region at a time of severely restricted access to finance.

Appropriate emphasis was given to policy dialogue too, especially related to the financial sector and in close cooperation with the IMF, central banks and regulatory authorities. The crisis had shown that a number of key areas such as bank insolvency rules, corporate governance and domestic capital markets had been found wanting.

An operational delivery Task Force involving the heads of all banking teams, as well as representatives from the credit, economics and planning departments, was swiftly set up under Varel Freeman, the First Vice President, to ensure that the Bank made good on its commitments. The Task Force met weekly throughout the crisis, reporting regularly to the Board on progress in the Bank's crisis response.

Graduation postponed

A stand-out element in the crisis response package was additional financing of €500 million the Bank had set aside for central Europe and the Baltics, precisely those countries from which the EBRD was supposedly stepping back ahead of their envisaged 'graduation' from the EBRD in 2010.

This chimed with demands from the more advanced countries themselves for which it was clear that this was not the time for the EBRD to start winding down its business. On 13 November, the Prime Minister of Hungary, Ferenc Gyurcsány, had written to the Bank's shareholders, saying,

> At this difficult juncture, we urge the EBRD … to strengthen its presence and, rather than investing less, to substantially step up its financing for Central Europe for as long as is necessary to help overcome the current crisis, preserve and consolidate the achievements of transition, and set our economies back on a path of recovery.[24]

24 Letter to Governors: Letter from the Prime Minister of Hungary, 17 November 2008.

Of the eight EU countries likely to graduate from the EBRD by the end of 2010, only the Czech Republic had done so—in 2007 before the full force of the crisis hit the region. Although the EBRD stuck to the principle of graduation, the lasting effects of the crisis postponed the remaining countries' graduation. Even now, over a decade later, these countries are still recipients of EBRD finance.

Financial institutions first

The Bank put an immediate focus on the worst hit areas. At the start of December 2008, Mirow made his first trip as EBRD President to Kazakhstan.

The EBRD also threw its weight behind Latvia, one of the worst hit countries whose GDP would drop by more than 20 per cent, saying it was looking to support systemically important banks that had no foreign strategic investors—banks like Parex Banka, in whose subsequent successful rescue and restructuring it would play a significant role (see Box 1).[25]

Another prominent locally-owned bank to benefit was Banca Transilvania in Romania, in which the EBRD had held a 15 per cent stake since 2001. The EBRD provided a €100 million loan. Nick Tesseyman, who had taken up the position of group Director for Financial Institutions in August, said, "In these exceptional global circumstances, the EBRD is using all available means to help shore up economic confidence in the region."[26]

Georgia's two largest banks, TBC and Bank of Georgia, were also a priority for the EBRD, since Georgia was now feeling the double impact of the crisis and the effects of the August 2008 conflict with Russia on its banking sector.[27]

Even as the EBRD was preparing for unprecedented levels of investments, management appeared confident that the Bank had adequate capital.

"No capital increase or any other additional contributions from the Bank's shareholders have been requested or are needed," a statement issued after the last Board meeting of the year said.[28]

---

25 EBRD Press Release, 15 December 2008. 'EBRD supports stabilisation efforts for Latvia'.

26 EBRD Press Release, 17 December 2008. 'EBRD supports Romanian small businesses with loan to Banca Transilvania'.

27 EBRD Press Release, 30 December 2008. 'Bank of Georgia to receive EBRD and IFC support'.

28 EBRD Press Release, 10 December 2008. 'EBRD Board adopts crisis response package'.

But at this stage the EBRD was still expecting positive growth ahead. The severe downturn in train would demand a far greater response than first anticipated.

Financing continued apace in 2009, in line with the promised crisis response. In the first three months of the year, new investments rose to €1.1 billion, up 64 per cent from the same period a year earlier and a record for any first quarter of the year since the Bank's inception.[29]

It would not be long before the Bank's corporate planners, and the President himself, realised an effective response to the mounting pressures on businesses in the region would require enhancements to the EBRD's capital base.

29 EBRD Press Release, 7 April 2009. 'EBRD investments hit record €1.1 billion in Q1.'

Parex Bank, Latvia

On the same day in April 2009 as it announced the rise in first quarter investments, the EBRD also unveiled its plans to contribute to the rescue of Parex Banka. This decision was not uncontroversial. The investment was deemed risky and fraught with potential political complications.

An earlier suggestion that the EBRD work with Parex had been rejected on integrity grounds. However, given its systemic importance as the second largest bank in Latvia (and largest Latvian-owned bank) with several subsidiaries in the Baltics and the Commonwealth of Independent States (CIS), and given the impact of the crisis, the EBRD decided to go ahead this time but only on the basis of a very tough stance on corruption and stringent governance guidance.

The EBRD team worked hand-in-hand with the IMF on the rescue of Parex. The fact that both institutions were taking part made it easier for each of the individual institutions to proceed.

The Latvian authorities had effectively nationalised Parex in November 2008, after a run on the bank linked to concerns about losses on its securities portfolio and its ability to repay two syndicated loans. The troubles in Latvia's banking system began earlier with some deposit outflows from Swedbank's Latvian subsidiary which were reversed when the Swedish government announced support. However, Parex did not have

a strong foreign parent company and its deposits were quickly haemorrhaging, with daily outflows peaking at €100 million a day, depleting deposits by more than one-quarter in the space of a few months.[30] The bank sought government assistance in late October and the state decided to take an initial 51 per cent controlling stake in November.

That was not enough to stem the run on deposits and the government then stepped in to buy up the remaining shares owned by the founders, Valerijs Kargins and Viktors Krasovickis, who received a symbolic one lat each.

For the EBRD, the investment in Parex Banka was critical to increasing confidence not just in the individual bank but also in the wider Latvian financial sector. It was supporting the recapitalisation of Parex and bringing its own expertise and reputation to strengthen the Latvian bank's corporate governance. The hope was that after a period of restructuring Parex might be privatised to a strategic investor. One of the key contributions of the EBRD participation in the Parex rescue was its intense lobbying to persuade the EU authorities to change their position and allow state aid to a bank.

The Board approved the EBRD's acquisition of a stake of a 25 per cent plus one share on 7 April 2009. The capital injection would give the EBRD representation on the supervisory board of Parex and a direct say in future developments, including in meeting anti-money laundering international best practices.

EBRD First Vice President Varel Freeman said the EBRD investment would "see Parex Bank through the most difficult time in its history". The Bank's involvement would help restore confidence in the bank and the whole Latvian financial sector. As a shareholder, the EBRD would be able to participate in the development and implementation of a strategic plan for Parex's restructuring.[31]

The purchase of the Parex stake became effective in September 2009. But much like other consequences of the crisis it was not the end of the story.

---

30 See 'IMF Executive Board Approves €1.68 Billion (US $2.35 Billion) Stand-By Arrangement for Latvia', IMF Press Release, 08/345, December 23, 2008.

31 EBRD Press Release, 7 April 2009. 'EBRD Board approves finance package for Parex Bank'.

Following discussions between the interested parties (Parex management and other stakeholders, the Prime Minister of Latvia and the EU Directorate-General for Competition), EBRD's investment was disbursed on condition that Parex would be split into a 'good' bank and 'bad' bank. The good assets and liabilities were to be spun off into a newly created bank, Citadele, owned by the Latvian Privatisation Agency, while impaired assets, syndicated loans and state funding remained in a bad bank branded Reverta. The split took place in August 2010 and the value of EBRD's investment was transferred to Citadele for a 25 per cent plus one share stake. Some further changes were made but delayed until the EC concluded the measures were in line with state-aid rules.[32]

The presence of the EBRD, alongside the significant restructuring, helped to make Citadele a privatisation candidate. As had been hoped for, a consortium of investors came forward in 2014, led by Ripplewood Advisors, a US investment company, and purchased the new bank. The EBRD remained a shareholder (with a stake of 25 per cent less one share), with its good knowledge of the bank and the Latvian market giving comfort to the new shareholder and its clients.

"The EBRD's investment in Parex and the policy advice we provided played a crucial role in Latvia's post-crisis macroeconomic adjustment," said Sabina Dziurman, the EBRD banker who led the work on the Parex investment. She added: "There is no doubt in my mind that we took a very large risk with an investment in a bank that was badly managed and poorly governed. But we persevered because this was a systemically important bank that was critical to Latvia's economic future. It was a risk worth taking."[33]

Citadele is today the fourth largest bank in Latvia with a successful track record and stands as a testament to the major effort by the EBRD, Latvian authorities and others in responding decisively to the crisis situation in 2008.

32 The matter was not resolved finally until July 2014.
33 Interview, January 2021.

6. High-level Coordination: The Vienna Initiative

The collapse of Parex during the autumn of 2008, and Latvia's negotiations with the IMF for support, came when there was a flurry of activity aimed at addressing the crisis but little by way of joined up thinking, a situation that Chief Economist Berglof saw as a major cause for concern. He warned repeatedly of the dangers of uncoordinated national responses to the crisis and the threat of regional systemic risks in emerging Europe.

Berglof and his colleagues were pioneers in a drive to plug a policy void that had undermined the coherence of many of the responses to the crisis. Together, they made sure that the EBRD played a significant role in the inception, roll out and management of a platform that would address problems in emerging Europe's financial sector.

According to one observer reflecting on this time:

> Piroska Nagy-Mohácsi and Erik Berglof of the European Bank for Reconstruction and Development (EBRD) ran around Europe trying to get something done. They proposed a public-private partnership to deal with the situation where no one cared about their neighbour and … everyone was focused on preserving their own country.[34]

There was no lack of activity at the time, with individual programmes of support from the IMF, the European Commission and others for the benefit of a number of countries hit hard by the crisis. Ukraine, Hungary and Latvia all benefitted from international sovereign support over the last three months of 2008.

In late November, the western European private sector piped up, with the heads of the six large EU-based banks most heavily engaged in central and eastern Europe[35] writing to European Commission President José Manuel Barroso and French Finance Minister Christine Lagarde (at the time Chair of the Economic and Financial Affairs Council of the EU). The bankers sounded an alarm bell about the state of financial stability in emerging Europe and pressed for liquidity injections, strengthened

---

34 Júlia Király, former Deputy Governor of the National Bank of Hungary, quoted in EIB, *Ten years of the Vienna Initiative, 2009–2019*, Vienna Initiative Steering Committee, 2019, p. 368. https://www.eib.org/attachments/efs/10years_vienna_initiative_en.pdf.

35 Erste Bank, Intesa SanPaolo, KBC, Raiffeisen Bank International, Société Générale and UniCredit.

deposit insurance, more IFI funding and for appropriate regulatory steps to be taken.[36]

The challenge, however, was to bring all these different initiatives together, to coordinate activities and to make sure there was a fair outcome for all concerned. The fear was that if the international banks with prominent subsidiaries in the region quickly withdrew to their home markets in western Europe, bank deleveraging would devastate central and eastern Europe's banking systems.[37]

At a conference at the EBRD's London headquarters in early December, the EBRD economists raised the possibility of a broader meeting that would address this issue of coordination and burden sharing, discussing the idea with Thomas Wieser, Director General of the Ministry of Finance of Austria. The aim of the meeting was to bring together the home and host supervisory and fiscal authorities of the large EU-based bank groups operating in emerging Europe and to forge agreement on the basic principles of information exchange, coordinated management of exposures and crisis burden-sharing.

On 23 January 2009, Wieser hosted a meeting at the Austrian Ministry of Finance in Vienna, with participants from the central banks and ministries of finance from seven central and eastern European 'host' countries and six advanced EU 'home' countries, and from the IFIs—the IMF, the EBRD, the EIB and the World Bank Group (including the IFC and the Multilateral International Guarantee Agency), as well as the European Commission.

Berglof initially labelled this platform for collective action between the public and private sectors the 'Vienna Club' (after the Paris Club). The formal title given to the platform was the European Bank Coordination Initiative, but it very quickly became known as the Vienna Initiative.[38]

---

36 'Stability for the Financial Sector in EU Member States and Candidate Countries', Letter from Andreas Treichl, Corrado Passera, André Bergen, Frédéric Oudéa, Alessandro Profumo and Herbert Stepic to Christine Lagarde, Manuel Barroso, Joaquin Almunia, and Charlie McCreevy, 1 December 2008.

37 Mark Allen in a comprehensive review of the chronology of the Vienna Initiative, on which this and the later commentary draws, notes: "From the time of the Latin American debt crisis of the 1980s, if not before, action to encourage creditors to maintain exposure and not to succumb to the temptation of withdrawing financing precipitately from a debtor country in distress had been a feature of the international handling of debt crises." Mark Allen, 'Ten years of the Vienna Initiative: a chronology', in EIB, *Ten years of the Vienna Initiative*, p. 16.

38 One close observer suggested the change of name to Vienna Initiative from Vienna Club to avoid any cynical connotation that the effort might be portrayed as a talking shop over tea and biscuits! The analogy with the Paris Club was apt however as the meetings required collective action between the interested parties (in this case non-binding agreements between public and private creditors) and regular meetings to forge consensus and actions. The London Club of private creditors (although moribund) was another angle.

As described by former IMF official Mark Allen:

> This was intended as a way to deal with the collective action problem among the banks, to send a signal to the markets and to allow the IFIs to complement each other's work. It was agreed that the IMF would draw up a proposal for burden-sharing rules between home and host authorities. Such a proposal was presented and broadly approved at a follow-up meeting of the group at the Joint Vienna Institute on 17 March 2009.[39]

At the heart of the matter was a tension between the international banks, who were under financial pressure and needed to meet constraints imposed by home supervisors, and thus wanting to protect their balance sheets as quickly as possible by cutting exposures, and host authorities who wished to ringfence and protect their domestic banking systems and stem capital outflows.

What the Vienna Initiative sought to solve was a classic coordination failure. Individually, an international bank may find it optimal to cut losses and withdraw from a crisis-hit economy, hoping that firms who borrowed from its subsidiary can repay by borrowing elsewhere. If all banks follow this strategy, however, firms may well be unable to roll over their debts. Defaulting en masse, they deepen the economic crisis, amplifying losses for the international banks. Much like banks in, say, Latvia had to be protected from a bank run by depositors in those depositors' best interest, whole economies needed to be protected from a bank run by international lenders.

The importance of the Initiative lay in:

> Arrangements with individual banks to maintain exposures as part of an international support package with the approval of their home authorities and to recapitalize subsidiaries should stress tests performed by the host authorities require it. These agreements to maintain exposure and capitalization were the central feature of the original Vienna Initiative.[40, 41]

39 Allen, 'Ten years of the Vienna Initiative: a chronology', p. 15.

40 Allen, 'Ten years of the Vienna Initiative a chronology', p. 16.

41 The Vienna Initiative website, http://vienna-initiative.com/about/vienna-initiative-1-0/overview/, cites the main initial objectives as: to prevent a large-scale and uncoordinated withdrawal of cross-border bank groups from the region, which could have triggered systemic bank crises not only in individual countries but in the region as a whole; and ensure parent bank groups maintained their exposures and recapitalise their subsidiaries in emerging Europe and that national support packages of cross-border bank groups benefitted their subsidiaries in emerging Europe and thus avoided a 'home bias'.

The EBRD took a group approach to lending to the banking sector, helping to shore up exposures of key western banking groups in the region by targeting their subsidiaries in a number of EBRD countries of operations. On 7 May 2009, for example, the Bank announced a series of transactions with UniCredit, an Italian bank and the largest banking group active in central and eastern Europe. It invested a total of €432 million in UniCredit subsidiaries across eight eastern European countries.[42] Similar support was provided for the subsidiaries in the EBRD regions of Paris-based Société Générale and Austria's Raiffeisen Bank International. Later, as south-eastern Europe fell prey to the unfolding Greek and eurozone crisis, the EBRD was to provide almost €1 billion of support for the banking operations of Greek banks which played a particularly significant role in the Balkans. (The EBRD's role in helping to ameliorate the Greek crisis is examined in Chapter 4.)

The Vienna Initiative sought to prevent a mass exodus from emerging Europe of precisely those banking groups that had such a dominant position in the financial sector of the region.

The foreign banks had a double-edged role in the run up to the crisis. Their investment had underpinned rapid economic growth, but this growth had turned into a liability once it developed into a surge and pushed loan-to-deposit ratios to exceptional heights—in most cases reaching well over 100 per cent and in Latvia touching 300 per cent.[43] As Croatian central bank governor and a later Vienna Initiative chair Boris Vujčić noted: "Part of the blame for the unsustainable expansion of CESEE countries rests with Western European banks."

The *quid pro quo* from the western European private sector to the pledges of liquidity and support from the public sector was that they should maintain their exposure in the region. In late March 2009, the CEOs of the parent banks began signing commitment letters pledging their support, initially for Romania and Serbia, and saying their banks would maintain their exposure and recapitalise their subsidiaries.

This was an agreement from which there could only be winners. As Vujčić pointed out 10 years later, the commercial banks were not acting out of pure altruism.

---

42 EBRD Press Release, 7 May 2009. 'EBRD and UniCredit join forces to support businesses across eastern Europe'.

43 See Figure 1 in World Bank and IFC staff, 'A perspective from the World Bank Group', in *Ten years of the Vienna Initiative*, p. 73.

> Due to the size of cross-border operations, for some banking groups large credit losses in the region could have jeopardized the solvency of the parent institution. In such a context, it was in foreign banks' best interest to keep supporting these economies. There was a case for coordination.[44]

Everyone involved recognised at the time that there would subsequently be a further restructuring and deleveraging within the region. Vienna, however, had made certain there was no uncoordinated stampede for the exit.

The Joint IFI Action Plan

A second key element within the Vienna Initiative was the Joint IFI Action Plan (JIAP) launched on 27 February 2009 by the EBRD, the EIB and the World Bank Group to channel €24.5 billion into the region over the following two years. Introduced just a month after the first Vienna meeting, the finance aimed to support the banking sectors in the region and to fund lending to businesses hit by the crisis.[45] The EBRD President explained how he saw the joint effort:

> The institutions are working together to find practical, efficient and timely solutions to the crisis in eastern Europe. We are acting because we have a special responsibility for the region and because it makes economic sense. For many years the growing integration of Europe has been a source of prosperity and mutual benefit and we must not allow this process to be reversed.

The EBRD hosted the secretariat of the Vienna Initiative from the outset and through its initial years. Given the number of actors involved—some 90 participants, including 15 systemically-important European banking groups active in the region, met at the first Full Forum—and the complexities of supervisory arrangements across multiple jurisdictions against a rapidly changing economic and financial backdrop, the Vienna Initiative was remarkably successful.

---

44 Boris Vujčić, 'Managing a supra-national public-private platform still based on sovereign interests', in *Ten years of the Vienna Initiative*, p. 5.

45 EBRD Press release, 27 February 2009. 'EBRD, EIB and World Bank Group join forces to support Central and Eastern Europe'.

A review in September 2009 concluded that reductions in cross-border exposures had been contained and financial conditions in CESEE stabilised. By the end of that month, the three IFIs had disbursed over €16 billion of support in the form of senior loans, tier 1 and 2 capital, trade finance, facilities for small business loans and syndicated loans.[46] The adjustment programmes, banking exposure agreements and JIAP financing succeeded in avoiding systemic collapse and restored confidence in CESEE financial systems. After severe recessions in 2009 most of the region's economies began to grow again in 2010.

In total more than €33 billion was delivered to the region by the end of 2010, well in excess of the original target. A report on the JIAP published in 2011 recorded that the EBRD's delivery too had exceeded its initial objective of a contribution to the JIAP of €6.0 billion, to reach a total of €8.1 billion.[47]

7. International Response and the EBRD

The 2009 Annual Meeting

As the months passed from the start of 2009 the true scope of the macroeconomic impact on the region was becoming clearer with every new assessment from the EBRD's economists. In January, they were no longer predicting growth of three per cent for 2009 but just 0.1 per cent. By May, they were expecting a contraction for the year of five per cent and, by the end of the year, they estimated that output would shrink by 6.3 per cent.

The priority for Mirow and his team now was to ensure that the EBRD was in a position to do whatever it could to make sure that the progress the region had made over the previous 20 years was not sacrificed to a crisis whose origin was not even of its own making.

With timing that could not have been more convenient, the Bank was about to embark on its regular five-year capital resources review (CRR), the fourth such review (CRR4), which was due to be discussed by Governors

46 Ralph De Haas, Y. Korniyenko, A. Pivovarsky, and T. Tsankova 'Taming the herd? Foreign banks, the Vienna Initiative and crisis transmission', *Journal of Financial Intermediation* 24, issue 3, 2015, p. 325–355.

47 EBRD, 'Final Report on the Joint IFI Action Plan', 2011, https://www.eib.org/attachments/final_report_on_joint_ifi_action_plan_feb_2011.pdf

in a year's time and cover the period from 2011 to 2015. There was no need for an immediate decision on resources as available capital was adequate in the near-term. But in a letter to Governors on 17 April 2009 previewing the upcoming EBRD Annual Meeting, Mirow warned that: "the Bank's capital and prudential ratios could impose constraints on the level of activity during the CRR4 period", and that the trade-offs between a higher crisis response, the effects of more impaired assets and capital requirements "will need to be evaluated".

Management prepared a paper entitled: "Fighting the Crisis, Promoting Recovery and Deepening Transition", which formed the basis for a Governors' discussion at the 2009 Annual Meeting in London. In keeping with the straitened economic backdrop to the event the meeting was held at the Bank's headquarters rather than in a central London hotel, as was traditionally the case when the EBRD staged its conferences in the UK and not in a country of operations.

The paper concluded that the EBRD's contribution to economic recovery had to draw on the lessons from the crisis. One such lesson was that building markets and promoting the private sector was not enough on its own. It was also important to improve the quality of those public and private institutions which supported markets and ensure that they worked well together.

Mirow wrote to the shareholders ahead of the meeting enclosing the paper, saying:

> These are not new insights, but the abundant liquidity of the past years allowed them at times to be sidelined. I propose to derive operational implications from these lessons for the Bank over the coming months, with a focus on the most effective ways to combine project finance, technical cooperation and policy dialogue.

The question of more intense support for policy development, the creation and strengthening of public institutions needed to introduce conditions more conducive to the promotion of the private sector and efforts to reinforce economic resilience featured prominently during the May discussions. In his summing up, Mirow told Governors in the closing session:

> I should like to mention the wish many of you expressed to see the EBRD engage more strongly in policy dialogue, for instance in relation to

> banking regulation and banking supervision. We take this very seriously. It will have an impact on the Bank's activities and probably also on how we finance this.[48]

Later, as staff ground through different business projections for the CRR4 period, and as demand for EBRD finance and help grew, it became obvious that shareholders would need to be primed for a change of heart on capital needs. Mirow and his team began to do just that.

The G7 and G20 meetings

As the EBRD worked on its own response to the crisis, individually and with partners in the context of the Vienna Initiative and the Joint IFI Action Plan, the G20 leaders were also developing their global response, which had direct implications for the multilateral development banks including the EBRD.

The G7 Finance Ministers under the chairmanship of US Treasury Secretary Henry Paulson had agreed a five-point plan of "exceptional action" to stabilise financial markets, restore the flow of credit and support systemically important banks back in October 2008,[49] following a week of dramatic stock market falls (of around 20 per cent) amid concerns that financial systems in the USA, and, especially, the UK, were on the point of collapse. This helped avert an immediate disaster.[50]

Nonetheless, it took a little while before international leaders fully understood the important role the IFIs could play—collectively as coordinators with convening power and financiers of last resort—in the face of a *global*, as opposed to domestic, crisis. UK Prime Minister Brown, Nicolas Sarkozy, the French President and Robert Zoellick, the World Bank President each called for an effort to create a new international financial architecture.

At the behest of the outgoing US President George W Bush, the first G20 Leaders' Summit was convened in Washington in November to consider the

---

48 President Mirow's closing speech to the Annual Meeting.

49 G7 Finance Ministers and Central Bank Governors' Plan of Action, 10 October 2008, Washington DC, Munk School, Trinity College, University of Toronto, http://www.g7.utoronto.ca/finance/fm081010.htm.

50 It gave time for the UK government to inject capital in exchange for equity in (most of) the main UK banks over the weekend of 11–12 October 2008. See Andrew Rawnsley 'The weekend Gordon Brown saved the banks from the abyss', *The Observer*, 10 February 2010, https://www.theguardian.com/politics/2010/feb/21/gordon-brown-saved-banks.

issues facing the international community. Encouragement was given to the MDBs to use their full capacity and ensure "[they] have sufficient resources to continue playing their role in overcoming the crisis".[51]

Spurred on by the gravity of the situation, Prime Minister Brown took the initiative to ensure that the proposed actions under the five principles agreed by the G20 were followed up by the relevant financial actors.[52] With the UK leading the G20 in 2009, he summoned the world's financial authorities to develop a fully-fledged international response—which in due course resulted in a global stimulus worth over US$ 5 trillion[53]—and one in which the IFIs, including the EBRD, were given a prominent role.

Following a round of visits to key capitals to win support for his plan, Brown chaired a G20 meeting in London on 2 April which reflected the spirit of cooperation and collaboration that had also been a hallmark of the Vienna Initiative. In their statement, the G20 leaders declared "a global crisis requires a global solution" and called for "systematic cooperation between countries" over regulatory systems.[54,55]

They made clear the MDBs were a key element in the global response: "We support a substantial increase in lending of at least [US]$ 100 billion by the Multilateral Development Banks (MDBs), including to low income countries, and ensure that all ... have the appropriate capital."[56] They agreed to "reviews of the need for capital increases" among MDBs, including for the EBRD.[57]

---

51 G20 'Declaration of the Summit on Financial Markets and the World Economy', 15 November 2008, Washington DC, Munk School.

52 The common principles for reform of the international financial architecture were: strengthening transparency and accountability; enhancing sound regulation; promoting integrity in financial markets; reinforcing international cooperation; reforming international financial institutions. See G20 Leaders' Declaration, 15 November 2008, Office of the Press Secretary, The White House, Washington DC, https://georgewbush-whitehouse.archives.gov/news/releases/2008/11/20081115-1.html

53 The headline at the time was a US$ 1.1 trillion boost to the IMF, trade and MDB finance. But allowing for the full effects of fiscal action the total was calculated at closer to US$ 5 trillion. See 'The April 2009 London G-20 Summit in Retrospect', Colin I. Bradford and Johannes F. Linn, Brookings, 5 April 2010 https://www.brookings.edu/opinions/the-april-2009-london-g-20-summit-in-retrospect/

54 'Global Plan for Recovery and Reform', Statement Issued by the G20 Leaders London, 2 April 2009.

55 Not all were fully satisfied with the G20 response (including Austria and Sweden who were not members of the G20). "Yet the G20 process left a gaping void. To be efficient it focused on the 'globally systemically important' economies, but abstracted from possible spill-overs and developments in countries of regional systemic importance." See Erik Berglof, Anne-Marie Gulde-Wolf, Piroska Nagy-Mohácsi and Thomas Wieser, 'Reflections on multi-country and multi-player issues' in *Ten years of the Vienna Initiative,* p. 53.

56 IMF Press Release, Leaders' Statement, 2 April 2009: https://www.imf.org/external/np/sec/pr/2009/pdf/g20_040209.pdf.

57 'Declaration on Delivering Resources through the International Financial Institutions', London, 2 April 2009, Munk School.

Only four months earlier, in December 2008, the EBRD had been confident that it could respond to the demands of the region without resorting to requests for further capital from its shareholders. But with the sizeable expansion of business volume and in a riskier environment, the question of adequate capital became much more pressing. By end-July 2009 commitments had exceeded €5 billion, the same as for the whole of 2008 and almost twice the amount achieved over the same period a year earlier, with some two-thirds deemed crisis-response investments. The rate of increase far exceeded the original estimate made by the Bank in its response to the earlier G20 call for a substantial increase in lending.

Meeting in London on 5 September, the G20 finance ministers and central bank governors acknowledged that the MDBs were fulfilling their side of the bargain and were "fully on track to deliver [US]$ 100 billion of additional lending".[58] Three days later, on 8 September, the EBRD announced a further increase in its planned investments for 2009. The Bank would now target €8 billion, a rise of another €1 billion and an increase of just over 50 per cent on the level of financing for 2008.

At a meeting in Pittsburgh on 25 September 2009, G20 leaders confirmed their position:

> We welcome and encourage the MDBs to continue making full use of their balance sheets … [and] …we will help ensure … the regional development banks have sufficient resources … including through a review of their general capital increase needs to be completed by the first half of 2010.[59]

8. A Contingent Callable Capital Increase

In a statement that September, the EBRD said it was acting in response to an appeal from the G20 for MDBs to make full use of their current capacity. However, while the rise in envisaged spending for 2009 would come out of reserves, the Bank indicated that it was indeed now looking at its capital base: "Additionally, and consistent with the appeal from the G20, the

58 'Meeting of Finance Ministers and Central Bank Governors, Communiqué', 5 September 2009, London http://www.g20.utoronto.ca/2009/2009communique0905.html.

59 'G20 Leaders' Statement: The Pittsburgh Summit', 25 September 2009, Pittsburgh http://www.g20.utoronto.ca/2009/2009communique0925.html.

shareholders of the Bank are reviewing the long-term capital requirements of the EBRD to ensure that it has adequate funding for the years to come."[60]

Mirow spoke more bluntly in two interviews that he conducted on the sidelines of a financial conference in the Plöner Schloss, a castle in the northern German state of Schleswig-Holstein. He told both *Reuters* and *Dow Jones* newswires separately that the EBRD could stretch to another €8 billion in 2010 on existing capital resources. But in the *Reuters* interview he said that the Bank "would probably go beyond the 8 (billion euros)," should there be a clear signal of support for a capital increase from contributing institutions and the international community. "In terms of a capital increase this would be a mix of callable capital and a very much smaller amount of paid-in capital. We cannot yet speak about concrete figures."[61]

Mirow declined to say whether its shareholders would provide the EBRD with more funds. "I would not speculate on that," he told *Dow Jones*. "We have to tell our shareholders what we can do with the existing capital and what is the potential. I think we have some good arguments to make."[62]

Towards the end of the month, Mirow outlined his proposals for a capital increase in a letter to shareholders that was quickly in the public domain. In the letter, Mirow warned that while the region's economies "had begun to stabilise" they had "not done so uniformly and it would be premature to say that a general turnaround has begun. The crisis will have lasting repercussions".

Writing 20 years after the fall of the Berlin Wall, Mirow said the region deserved broad support in continuing "its mutually beneficial integration into the European and world economies". A €10 billion capital increase to €30 billion would allow the Bank to commit €9 billion to €10 billion annually, or €20 billion in total extra funding during the next five years, 2011-2015. Allowing for the mobilisation of additional capital from private investors, Mirow pointed out that the extra funds could reach €60 billion.

In his letter, Mirow also raised the prospect of a change in the development model of the region, in which there would be less dependence on foreign capital and a greater reliance on its own resources.

60 EBRD Press release, 8 September 2009. 'EBRD ups investments to €8 billion in 2009'.

61 'EBRD: East European investment at least 8 billion eur in 2010', *Reuters News*, 11 September 2009.

62 Nina Koeppen, 'EBRD Could Raise Investments With New Capital', *Dow Jones Newswires*, 11 September 2009.

> The region will need to change its growth model—away from a reliance on easy finance and commodities, and towards the development of domestic financial markets, strong institutions and a diversified production base.

Commenting on the proposals, the *Financial Times* said:

> Mr Mirow's proposals highlight how the global recession has transformed the EBRD. Before the crisis, the US, the biggest shareholder, was keen to reduce the bank's activities on the grounds that its role in supporting post-communist transition would end as the market economy took root in region. But following the crisis, and Barack Obama's election as president, Washington has developed a more positive view of international financial institutions, including the EBRD. However, Mr Mirow remains sensitive to possible complaints from shareholders that bank executives may be taking advantage of the crisis to reinforce it as an institution.[63]

Shareholders formally approved the €10 billion capital increase at the EBRD Annual Meeting in Zagreb, Croatia, on 14 May 2010.

French Finance Minister Christine Lagarde, Chair of the EBRD Governors for that year, praised the structure of the transaction as "innovative in at least two ways":

> Firstly, it combines a rise in callable capital of €9 billion with a transfer of €1 billion of reserves to capital and secondly, it includes provisions to review the use of this capital after five years. I am very happy that the EBRD is demonstrating an exemplary sense of responsibility in the utilisation of its resources.[64]

The EBRD was able to scale up its activities but without putting any immediate strain on government coffers as the additional finance was primarily in the form of callable capital, with the rest taken from reserves that had been built up in good times (and, fortuitously, not depleted through a payment of dividends).

---

63 Stefan Wagstyl, 'EBRD seeks 50% increase in capital', *Financial Times*, 28 September 2009. https://www.ft.com/content/a0dffec0-ac51-11de-a754-00144feabdc0

64 EBRD Press release, 14 May 2010. 'EBRD shareholders boost capital, pave way for increase in investments'.

After record lending commitments of €8 billion in 2009, annual business volume increased further to €9 billion in both 2010 and 2011.

9. A Focus on Local Financial Markets

Ahead of the Zagreb meeting, the EBRD President used a speech at the London School of Economics (LSE) to raise the prospect of a 'New Growth Agenda' for emerging Europe that would help deal with the imbalances and weaknesses in the region's economies that had been laid bare by the crisis.

In his speech, Mirow again focused on the mismatch between external and domestic sources of financing and the need to promote further diversification of economies. Excessive reliance on foreign credit and borrowing in foreign currencies had emerged as one of the largest weaknesses in the region. Mortgages and loans for cars and other goods had appeared cheap at the low borrowing rates in the Swiss franc or Japanese yen. But they very quickly became unaffordable liabilities once local currencies came under pressure.

In Zagreb, the EBRD delivered its response to the challenge of foreign currency dependence when it unveiled a Local Currency and Local Capital Markets Initiative that sought to promote the use of local currency within a wider macroeconomic and regulatory framework that ensured sustainable and liquid markets for long-term funding in local currency.

Launching the new programme, Berglof said:

> The crisis laid bare the region's twin vulnerabilities of excessive reliance on foreign capital and excessive use of foreign exchange borrowing. As the recovery takes hold in the region, it is important to urgently address these vulnerabilities, with a fresh eye and approach that fuses the knowledge and expertise of key stakeholders: governments, IFIs, the banks and other private sector stakeholders.[65]

The new programme put local currency lending and local capital market development firmly on the EBRD's agenda. The Bank had already borrowed and lent in local currency—as early in 1994 when it conducted transactions

65 EBRD Press release, 14 May 2010. 'EBRD shareholders boost capital, pave way for increase in investments'.

in Hungarian forint. But the initiative took these activities to a completely new level. (The initiative is considered further in Chapter 8.)

10. 'Vienna Plus' and the Vienna Initiative 2.0

The Vienna Initiative had been an unqualified success and questions turned naturally towards next steps as the second Full Forum approached in the spring of 2010. There was no doubt that it had filled a hole in the European financial architecture. It was clear too that no other body or institutional setting was in place ready to take on its mantle. The Forum thus agreed to maintain the arrangements in view of the continuing vulnerabilities facing the region.

The focus now turned from crisis resolution and towards crisis prevention and led to what became known as "Vienna Plus". Two working groups were set up to deliver improvements in new areas, again involving public and private sector participants. One group, chaired by the EBRD, looked at problems in local currency and capital markets; while the other group, led by the EC, concentrated on the role of commercial banks in the absorption of EU structural funds.

The crisis had revealed many weaknesses in the transition economies and led to major reflections on the implications for the emerging markets' growth model.[66] One important conclusion from this work concerned the vulnerabilities created by foreign currency lending in the EBRD's countries of operations and the need to boost domestic savings. The Bank had begun work on strengthening local currency and capital markets to draw attention internally to the problems that would need to be tackled in Bank operations in future.[67] The opportunity to work with banks, regulators and finance authorities across Europe under the Vienna Initiative umbrella fitted well with these objectives.

The working group reported in November 2010. It recognised the need for greater reliance on domestic savings, especially in domestic currencies, and made a number of recommendations, including tighter prudential requirements on foreign currency lending, greater local currency sovereign issuance and macroeconomic policies designed to support local

66 See Chapter 6.
67 See Chapter 8.

currency market development. The other working group suggested ways in which commercial banks could facilitate the use of EU structural funds. This was especially relevant to countries like Bulgaria and Romania where low absorption of these funds was particularly acute.

The third Full Forum in March 2011 introduced two further working groups, one on the implications of implementing Basel III regulations in emerging Europe (these were seen as a tightening of the regime), and the other on non-performing loans (NPLs) in CESEE.

During this time, the crisis in Greece was deepening and spreading to other highly indebted European countries, notably Ireland, Portugal and Spain. Most large European banks held significant amounts of sovereign debt of these countries, and this engendered a so-called 'doom-loop' as banks' assets fell in value while increasing precariousness of banks' balance sheets gave rise to concerns about forthcoming bank rescues. Those concerns, in turn, drove up yields on sovereign debt further depressing the value of bank holdings of sovereign paper.

Funding conditions worsened and national regulators pushed the parent banks to strengthen their balance sheets and raise capital. Banks operating in CESEE once again faced difficulties raising finance. The home bias of regulators—their tendency to favour banks' lending within their jurisdictions over lending abroad—threatened to undo progress made under the Vienna Initiative.[68]

Towards the end of November, Berglof pressed the case for a renewed effort, a Vienna Initiative 2.0, in order to address the external risks and deleveraging once again facing the CESEE region.

The same players from the private and the public sectors met in Vienna in early January 2012 to consider the situation. At the meeting, they agreed a set of principles for coordination between supervisory authorities of home and host countries, including on the free allocation of liquidity and capital and consideration of spill-overs from national actions,[69] and launched the Vienna Initiative 2.0 at the fourth Full Forum meeting in March.[70]

68 Among the concerns was a decision on 21 November 2011 by the Austrian authorities to increase capital requirements and introduce tighter lending criteria on cross-border activities by their banks.

69 Joint Press release, 13 March 2012. The Forum described the effort as "designed to enhance cooperation and coordination among the various stakeholders so as to help ensure mutually beneficial outcomes even in times of global financial stress and a shifting financial-sector landscape." http://vienna-initiativ e.com/wp-content/uploads/2012/08/Principles-for-Home-Host-Authority-Coordination.pdf.

70 The meeting also adopted reports from the working groups on Basel III and non-performing loans, embrac-

This second iteration of the Vienna Initiative was more structured with a Steering Committee headed initially for a five-year term by Marek Belka, who at the time was Governor of the National Bank of Poland. He was well-qualified for the role. Belka had been the Director of the IMF's European Department and a key ally of the EBRD in the early stages of the crisis, and played a key role as chair of the Vienna Initiative in driving forward international coordination.

With the eurozone crisis intensifying and affecting the economies of CESEE negatively—eight out of 17 countries in CESEE experienced falls in GDP in 2012[71]—and with cross-border deleveraging once again threatening these countries' financial systems, the World Bank Group, EIB and EBRD announced a new Joint IFI Action Plan for Growth for the region, pledging to provide over €30 billion of new resources for infrastructure and the corporate and financial sectors in 2013 and 2014.

The final tally of €42.7 billion far exceeded the original estimate, with the EIB providing the largest amount at €28.3 billion and the EBRD at €7.0 billion the biggest proportional increase (up from an originally estimated €4.0 billion).[72] According to the final report on the Joint IFI Action Plan for Growth, "assistance from the IFIs was in the order of 1½ per cent of the region's GDP each year, and supported around 6 per cent of the region's investment."[73]

By 2014, growth had returned to nearly all countries in the region.[74] As had been the case previously, the rapid and substantial countercyclical financial support from the IFIs proved to be a timely input in a difficult situation.

The pioneering Vienna Initiative had fended off the potential for dual financial and currency crises across the region on more than one occasion.[75]

---

ing recommendations on ways to include emerging market concerns more effectively in regulatory debates and remove impediments to NPL resolution.

71 The 17 countries comprise EU member states, Bulgaria, Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia and Slovenia and EU candidate and potential candidate countries in the West Balkans such as Albania, Bosnia and Herzegovina, Kosovo, North Macedonia, Montenegro, and Serbia. Those with negative growth in 2012 were: Croatia, Czech Republic, Hungary, Slovenia, Bosnia and Herzegovina, North Macedonia, Montenegro, and Serbia.

72 World Bank Group, EIB and EBRD, 'Final Report on the Joint IFI Action Plan for Growth in Central and South Eastern Europe', 2015, Table 1, p. 5, https://www.eib.org/attachments/efs/economic_report_jiap_IV_2015_en.pdf.

73 'Final Report on the Joint IFI Action Plan for Growth in Central and South Eastern Europe', p. 19.

74 Of the 17 countries only Croatia and Serbia registered negative growth in 2014, of -0.3 and -1.6 per cent, respectively.

75 Subsequent work under the Vienna Initiative umbrella paid increasing attention to the concerns of south-eastern Europe (SEE), whose countries were candidates or potential candidates for EU membership, and included the appointment of a representative from the region to the Steering Committee (initially the Gover-

It had been a major success for the EBRD and, in particular, for its Chief Economist. The CEO of Erste Group, Andreas Treichl, put it this way:

> The Vienna Initiative was more than a success. No country in the [CESEE] region required any support to its banking system—the whole region was kept clean of government support, a huge success. It is a wonderful story to tell regulators in Brussels. A case of professional people getting together to solve a problem and having the guts to do it.[76]

11. The Crisis and the Transition Development Model

Within months of the beginning of the crisis, Berglof and his team of economists embarked on a long, hard look both at its impact on the region's economies and the entire paradigm upon which the operationalisation of the EBRD's mandate was based.

One outcome of this work was a detailed report[77] published a year after the onset of the crisis. It raised questions about the development model for transition, especially the financial integration that had fuelled rapid expansion, and how to deal with countries, particularly further to the east, whose growth depended on income from natural resources. According to Zettelmeyer, the main editor of the report, the crisis challenged everything the EBRD had worked for up until then:

> It challenged the very paradigm of financial integration. The paradigm that integration was a good thing was something we had written on our flag. That was the core ideology of EBRD—right below the idea of transition itself.

---

nor of the Bank of Albania, Ardian Fullani, and then the Governor of the National Bank of the Republic of Macedonia, Dimitar Bogov). This raised these countries' profile and an opportunity to hear and learn best practices as new supervisory and regulatory arrangements came into play. As small countries outside mainstream European banking structures yet with sizeable dependence on eurozone banks (with consequential spillovers outside their control), the Vienna Initiative served their interests well over the longer term, just as it had done in the immediate aftermath of the crisis. *Note by authors*: In 2019, the National Bank of the Republic of Macedonia changed its name to the National Bank of the Republic of North Macedonia.

76 EIB, *Ten years of the Vienna Initiative, 2009–2019*, p. 370.

77 'Transition in Crisis?', EBRD *Transition Report 2009*.

A close look at financial integration made clear that the model was a double-edged sword. On the positive side, the report declared "financial integration has significantly benefitted the transition region by contributing to high economic growth over at least a decade", and attributed the relative success of CESEE transition countries to their deeper integration with advanced countries and the role of foreign-owned banks.

On the other hand: "Financial integration may also have had significant costs, in terms of encouraging credit booms and overborrowing, and possibly in biasing the denomination of borrowing towards foreign currency."[78]

Some of this inevitably reflected the process of integration, the authors noted, and by helping deepen financial systems the foreign banks may have had a longer-term stabilising influence. The report concluded that it would be wrong to try to end or reverse financial integration, even if it was possible, as this would "deprive [the region] of a source of growth".

Berglof was nonetheless in no doubt that the transition region was in deep crisis. In a foreword to the *Transition Report 2009*, he asked whether transition itself was in trouble:

> How have the institutions and policy frameworks that were the outcome of the transition process coped? Are the ideas that drove transition, which in addition to market reforms and trade integration also encompassed financial liberalisation and integration, still attractive? Lastly, is the future of transition in doubt? Will the crisis lead to a backlash against market-oriented reforms?[79]

Berglof responded to his own question—answering that posed by the title of the report, "Transition in Crisis?"—with what he said was a "qualified no". The global recession had "demonstrated the resilience of reforms and economic integration" achieved over the previous two decades. But it had highlighted "some pitfalls of the development models that countries in the transition region have pursued." Berglof concluded: "... it is clear that the way to address these pitfalls is to extend the transition agenda, not to replace it."[80]

---

78 'Transition in Crisis?', EBRD *Transition Report 2009*, p. 73.
79 'Transition in Crisis?', EBRD *Transition Report 2009*, p. vi.
80 'Transition in Crisis?', EBRD *Transition Report 2009*, p. vii.

From this point on, the EBRD continued to pursue market-oriented solutions but paid closer attention to the distinct role of the institutions underpinning markets—especially to the need for effective state, legal and regulatory processes—and to market-enabling qualities successful transition needed to encompass.

The thinking behind a deeper interpretation of transition and operational procedures was as yet in its infancy and it would take some time before the transition concept was fully updated.[81] Views on how the EBRD should implement its mandate and its newfound enhanced role were however about to receive a significant impetus from another crisis emerging on its southern borders. One in which the EBRD would again be called upon to play its part: the "Arab Spring".

81 See Chapter 6.

Chapter 3
Arab Spring

Introduction

When the EBRD started operating in Turkey in 2009, the Bank's management and its shareholders were keen to stress that it was not a precedent for rapid further expansion. It was introduced very much as a one-off step, with Turkey the obvious gap in a region that spanned Europe and Asia. There was a clear logic in developing a continuum of coordinated economic integration.

That the EBRD might venture across the Mediterranean—into a third continent—to embrace yet more economies that were culturally and historically distinct from its traditional post-communist, east European stamping ground was not seriously on most shareholders' agenda.

Yet, just as the EBRD had been born out of a huge and sudden sweep of socio-political change across an entire region, it was another tsunami of demands for democratic freedom, dignity and economic improvement that triggered the next move.

Those demands started with the suicide on 17 December 2010 of a Tunisian street vendor who could no longer stomach his daily ration of harassment and humiliation from public officials. In response, protests spread across Tunisia and then right across North Africa and into the Middle East, toppling some autocratic leaders and securing pledges of economic and political reform from others.

The EBRD would very quickly become part of the response of the international community to calls to support this new wind of change, the 'Arab Spring'. That had not been on the cards when Governors gave a green light for a review of expansion to Turkey at the 2008 Annual Meeting in Kyiv. The refrain there had been "Yes to Turkey. And no further".

Three years later, meeting in the then Kazakh capital Astana,[1] Governors gave the EBRD the go-ahead to embark on another journey to a new geography, the southern and eastern Mediterranean. For the EBRD, 21 years on from the creation of its charter, it was as much a rebirth as a coming of age.

The Middle East and North Africa (MENA) had traditions in many ways vastly different to the legacy of the Soviet communist era encountered initially by the EBRD. Its young and fast-growing population, poor regional integration and long-standing and deep cultural heritage contrasted with the Soviet experience. But there were commonalities too, in the need to break the stranglehold of state regimes—whether bureaucratic, militaristic or monarchist—find productive jobs for a well-educated but underused workforce, and introduce democratic freedoms so long suppressed by feather-bedded plutocrats.

It was indeed a new challenge for the EBRD. But it was one that was entirely in keeping with its transition mandate.

1. Before the Arab Spring

Egypt's early request

At the 2008 Annual Meeting in Kyiv, when most delegates said there should be no further expansion beyond Turkey, one voice stood out from the crowd.

Fayza Aboulnaga, Planning and International Cooperation Minister under Egyptian President Hosni Mubarak, said Egypt supported Turkey's change of status and saw it as a "positive precedent," adding:

> As Europe extends partnership and the EuroMed union to the south, southern partner countries that are EBRD members, such as Egypt, are also eligible to benefit from the Bank's assistance and operations.[2]

She repeated the call the following year, when the EBRD was holding its Annual Meeting in London, the first under the presidency of Thomas Mirow. Aboulnaga spoke of the effort Egypt had been putting into

1 On 20 March 2019, the capital was renamed from Astana to Nur-Sultan.
2 Speech to 2008 Annual Meeting.

delivering economic and social reforms. But the country still faced a number of challenges:

> The Egyptian economy therefore remains in need of the EBRD's unique set of skills and experience that the Bank has built up over 18 years of helping countries of operations develop market economies and strengthening private enterprises, especially in light of the global financial crisis, which is turning into a real economic crisis.[3]

With operations in Turkey growing and the global financial crisis affecting all economies, including Egypt, the call became formal in 2010 when shareholders met in Zagreb to agree a 50 per cent capital increase to bolster the Bank's resources to stave off the impact of the crisis. Aboulnaga presented Egypt's case to the assembly:

> As a founding member of the EBRD, Egypt is quite familiar with, and indeed appreciative of, the Bank's support to its countries of operations—including its role during the crisis—and thus we strongly believe that extending the EBRD's operations to Egypt would support our development endeavours.

She listed the areas where the EBRD could be particularly useful with its specialised skills and expertise, in sustainable energy, climate change mitigation, information and communication technology, infrastructure and agribusiness:

> Changing the status of Egypt to an EBRD country of operations is in our view a win-win prospect, as it will definitely generate benefits for Egypt as well as for the Bank and its members.[4]

Closing the Annual Meeting, the Vice Chair of the Board of Governors, Slovak Finance Minister Ján Počiatek, was non-committal but said, "...the interest in becoming a country of operations expressed by Egypt and,

---

3 Speech to 2009 Annual Meeting.
4 Speech to 2010 Annual Meeting.

possibly, other countries, will need analysis and discussion".[5] "Other countries" referred specifically to Morocco, another founding shareholder of the EBRD. The Alternate Governor from Rabat, Abdeltif Loudyi, had aligned his authorities with Egypt telling the conference: "Joining the countries of operations affords an opportunity for our two countries, Morocco and Egypt, to benefit from the expertise acquired by the Bank in specific areas."[6]

The Zagreb Annual Meeting triggered a review process for Egypt's request. Mirow told journalists at the end of the conference that the EBRD would certainly look into the Egyptian request. "What I've said here to the Board of Governors is that they deserve a serious consideration," Mirow said. But he was making no promises. "We will need to make an assessment of any possible step and then put this on the table for discussion ... I made a commitment in procedural terms but made no commitment in substantial terms."[7]

France considers a European Mediterranean Bank

Just as the EBRD was preparing its response to Egypt, even if there was little real sense of where the review might end, the Bank was drawn into a parallel debate about European development plans for the Mediterranean region.

A French-led initiative was looking into the creation of a European-Mediterranean (EuroMed) Bank that appeared to be developing in the image of the EBRD itself. The proposed bank was a product of the 43-nation Union for the Mediterranean (UfM), a brainchild of French President Nicolas Sarkozy. Launched in 2008, the aim of the UfM was to create a more balanced dialogue between the wealthy EU and the poorer states that line the Mediterranean including in North Africa and the Middle East.

One year later, Sarkozy wanted to back up that dialogue with financial support. He charged Charles Milhaud, former Chairman of the Board at the Caisse Nationale des Caisses d'Epargne, the French mutual banking group, with forming a Working Group to "assess the opportunity of creating a bank dedicated to the financing of co-development in the Mediterranean".

Milhaud's group comprised high-ranking officials from both sides of the Mediterranean, and included a Vice President of the European Investment

5 Closing address to 2010 Annual Meeting.
6 Speech to 2010 Annual Meeting.
7 'EBRD increases 2010 growth forecasts for Eastern Europe', *Dow Jones*, 15 May 2010.

Bank (EIB), Philippe de Fontaine Vive Curtaz, as well as Jean Lemierre, the former EBRD President and then Adviser to the Chairman of BNP Paribas.[8]

Milhaud's report was published in May 2010. It recommended the creation of a Euro-Mediterranean financial institution for co-development, by establishing a dedicated subsidiary of the EIB, encompassing the EIB's existing Mediterranean activities which were then headed by de Fontaine Vive.[9]

The attributes of the institution they were proposing tallied closely with the programmes and instruments the EBRD had been applying to its regions over the previous 20 years. The report said:

> This new institution would focus on supporting the private sector, in particular through assistance for long-term financing, helping SMEs gain access to bank credit, developing guarantees, stimulating financial markets, supporting innovative investment funds and transferring financial technology through technical assistance.

It added:

> The value of any new institution would be conditional upon the implementation of institutional and economic reforms propitious to private initiative. It should have a complementary role, offering services that other institutions do not provide to any great extent or very well, without worsening coordination issues. It should be subsidiary to the private sector and not replace it; finally it should be an instrument of transition and support.

The report, which proposed the EIB as the "reference shareholder" of the new institution, taking approximately one third of the bank's capital, was presented to Sarkozy in August. Media speculated at the time that de Fontaine Vive would be tapped to lead the Euro-Mediterranean Bank. There was also media speculation of German opposition to the project.

In an article headlined "Berlin Risks Burying Milhaud Report," *Maghreb Confidential* wrote:

---

8 Lemierre would later take the Chair of BNP Paribas.

9 'The Financing of Co-Development in the Mediterranean', Final Report, May 2010. https://www.bassanini.it/wp-content/uploads/2020/10/Final-Report.pdf.

> Some fear Germany could torpedo France's hopes of setting up a Union for the Mediterranean "bank" … According to our sources, the German government doesn't seem keen on having 43 countries—members of the Union for the Mediterranean—having a say in decision-making at the bank.[10]

At the EBRD, there was sufficient interest in the project—even from a distance—to consider the implications of the creation of a new financial institution very similar to the Bank itself. Mirow dispatched his head of office Hans Peter Lankes to a meeting on the new bank as an observer.

An EBRD "non-paper"[11] looked at whether there might be a possible role for the EBRD in the Mediterranean and noted the similarities between the objectives and characteristics of the proposed new bank and the EBRD. These included "co-development"—the principle of joint ownership and determination by recipient and donor countries that was core to the EBRD's own model—as well as the new bank's focus on creating sustainable jobs via the private sector. Other key principles of the new bank like conditionality, complementarity with other IFIs, subsidiarity vis-a-vis the private sector and a transitional mandate were all part of the EBRD model.

The paper concluded that the EBRD could indeed fill an important gap in the financial architecture of the region, as part of a well-designed division of labour with the EIB and other development lenders. But it made equally clear that it only intended to contribute to the current debate. It was not a proposal and did not necessarily reflect the views of the Board and shareholders of the EBRD.

This debate was taking place just as the EBRD, in late 2010, was preparing its response to the request from the Egyptian authorities, as had been agreed at the Zagreb Annual Meeting. A draft work programme on Egypt was circulated to the Board in November, identifying a division of labour within management and listing issues that needed to be assessed, including the legal, economic and operational implications. That work was expected to be completed roughly one year later, in October or November 2011.

---

10 *Maghreb Confidential* report, 28 October 2010.

11 A "non-paper" is a document written by officials offering views which are not a formal position of an organisation.

2. The Arab Spring and Preparations for an EBRD Response

Tunisian street vendor's protest triggers a revolution

Work on the EBRD's response to Egypt and the elaboration of plans to create a new EuroMed bank suddenly and dramatically took on a new complexion, as a result of the death of the Tunisian fruit seller that triggered an explosion of protest across the Arab world.

Mohamed Bouazizi set himself alight on 17 December 2010 after facing yet more intimidation. Suffering from horrific burns, he finally died in hospital on 4 January 2011. Bouazizi became a *cause célèbre* for the people of Tunisia who sought dignity, rights and justice, and an end to humiliation and suffering. His solitary act of defiance unleashed a chain of popular revolt, first in Tunisia and then across the Arab world.

Protests spilt over to engulf Egypt, Syria, Yemen, Libya, and the monarchies of Jordan and Morocco, in what became known as the Arab Spring or Arab Uprising.

In Tunisia, the revolts spread rapidly through the whole country. On 13 January 2011, just days after Bouazizi's death, hundreds of protesters ignored a curfew and fought running battles with police in the centre of Tunis. One day later, after dissolving his government and declaring a state of emergency, President Zine El Abidine Ben Ali, who had ruled over Tunisia since 1987, fled to Saudi Arabia.

On 17 January, a man in Egypt set fire to himself outside the parliament building in Cairo. Others followed suit in what appeared to be echoes of the Tunisian suicide of one month earlier. Just days later, demonstrators were gathering in their thousands in the Egyptian capital, clashing with police who responded with tear gas and water cannon. 25 January was known as 'The Day of Revolt.' 28 January erupted into a 'Friday of Anger.'

Cairo's Tahrir Square became a scene of violent clashes between the demonstrators and Mubarak supporters and the security forces.

The 18-day revolution ended on 11 February, when Mubarak handed over power to the military, leaving the Egyptian capital for the Red Sea resort of Sharm el-Sheikh. A statement from the military said the current government and regional governors would "act as caretakers of all businesses until a new government is formed". It would look to guarantee "a peaceful transition of authority in a free democratic framework which

allows an elected civilian authority to rule the country, to build a free democratic country".[12]

US President Barack Obama hailed the event as a display of "the power of human dignity" and called on the Egyptian military to devise a clear path to fair and free elections that would make the transition "irreversible".

Even before the removal of Mubarak, the request from the Egyptian authorities to the EBRD had taken on a new dimension as the world witnessed the people of a region demanding radical change. There was an unmistakable echo of the events of eastern Europe two decades earlier.

The EBRD considers Egypt's request in a new light

When the Board met on 1 February 2011 to discuss the Egyptian work plan, it was against the radically changed backdrop of popular revolt on the streets of Cairo and other major cities. There was a new sense of urgency to the Board discussion, even though Mirow knew he had to be cautious about raising excessive expectations on behalf of the Egyptians and putting pressure on shareholders when the situation in the region remained unclear.

Some Directors had asked for the session on Egypt to be postponed. Mirow believed this would be a mistake, saying the EBRD had to be prepared to respond to changing circumstances. He conceded in his remarks to the Board that the situation in Egypt was fluid. However, he predicted that there might soon be a need for the international community, including EBRD shareholders, to engage rapidly and strongly. By then the EBRD needed to be ready. Any decision by shareholders should not be held up by an avoidable lack of preparation. Mirow circulated an updated timetable for the Egyptian review.

Views of the EU High Representative

The following day, Mirow shared the Bank's reflections with Baroness Catherine Ashton, who had been appointed in 2009, on the recommendation of the UK Prime Minister Gordon Brown, as the EU's first High Representa-

12 "Egypt military pledges transition to civilian rule," *BBC*, 13 February 2011, https://www.bbc.co.uk/news/world-middle-east-12441771.

tive of the Union for Foreign Affairs and Security Policy.[13] She was spearheading the EU's response to the fast-moving events in the Arab world.

In his letter, Mirow was replying to Ashton's interest in clarifying the possible response of the international financial institutions to developments in North Africa. He made clear that the EBRD was reviewing the Egyptian request and that preliminary findings should now be available in the spring—not towards the end of the year as envisaged under the earlier work plan. He included the caveat that any decision to engage in Egypt would require unanimous support from the shareholders.

Already in February, the EBRD was considering possible ways of moving very quickly to deliver funding to the Arab region. While unanimous support was needed to open up the region to full-scale EBRD investment, the creation of a Special Fund for investment would need a lower threshold of support and could probably be achieved more quickly.

Mirow drew on the EBRD's most recent experience in the expansion to Turkey, where annual investments were set to rise to around €1 billion after just three or four years in the country. A similar-sized engagement was possible for Egypt.

Ashton reached out publicly to the EBRD on 14 February in an impassioned article for the *Financial Times*, entitled "Europe's downpayment on democracy".[14]

Scenes of jubilation from Tunis and Cairo had brought to mind earlier successful conquests of tyranny, whether in Paris in 1944, in Gdansk in 1980 or across eastern Europe in 1989, Ashton wrote. The EU stood ready to help, she said, and asked the EIB to mobilise €1 billion for 2011, initially for Tunisia. She explained she would call on member states to free up another €1 billion, to support democratic reform including in Egypt.

Ashton directly invoked the EBRD. In an apparent reference to the plans to create a new EU Bank for the Mediterranean, she continued:

> Rather than reinvent the wheel, we need now to give these structures the new task of supporting the current democratic wave. If shareholder

---

13 The Prime Minister's Sherpa, Jon Cunliffe, was a former EBRD Alternate Director and knew the EBRD's attributes well, and its potential in the circumstances. Like Ashton, he was heavily engaged with key officials involved, in this case working closely with France and the USA in preparing both a G8 and G20 response.

14 Catherine Ashton, "Europe's downpayment on democracy," *Financial Times,* 14 February 2011, https://www.ft.com/content/6f5fcc40-387d-11e0-959c-00144feabdc0.

> countries agree, the EBRD could—with its existing resources—provide at least €1bn of finance annually to underpin the transition in Egypt, for example. I shall shortly travel to Cairo to find out what the outside world can do to help. I shall work with other EBRD shareholders around the world to build agreement for this.

EBRD Press Officer Axel Reiserer confirmed to the media on 15 February that the EBRD was aiming to finalise the technical study on Egypt by the spring. He said there had been no request by shareholders to speed up the formal processes; while there was political momentum and a sense of urgency the legal requirements on any decision remained the same.[15]

Different visions of financial support

That same day, the EIB's de Fontaine Vive was continuing to raise the profile of the possible new EU Bank for the Mediterranean and the role it could play in financing for the Middle East and North Africa. He referred to calculations made for French President Sarkozy, who had championed greater EU support for the bloc's Mediterranean neighbours, showing the new co-development facility could generate €10 billion of business a year. De Fontaine Vive said support for such a bank appeared to be growing, despite earlier resistance from northern European states.[16]

Mirow chose Oxford University as a venue to outline his own vision for the role the EBRD could—once again—play to support a whole region that was crying out for change.

There were clear parallels with the events of 1989 that had catapulted the EBRD into existence. The world was once again at a historical turning point. Reflecting on the point, Mirow said in his speech on 23 February to the Oxford International Relations Society: "What we saw then and what we are again witnessing today is people's thirst for freedom, self-determination and democracy."

Mirow pointed to the huge expertise the EBRD had gathered in the two decades in eastern Europe. This was experience that could "travel beyond

15 'EBRD aims to complete Egypt inclusion study by spring', *Reuters News*, 15 February 2011, https://www.reuters.com/article/uk-egypt-ebrd-idUKTRE71E4OB20110215.

16 'New EU bank could quadruple North Africa, Middle East aid', *Reuters News*, 15 February 2011.

our existing areas of work". Analysis of what the EBRD could do in Egypt was now proceeding apace and he confirmed the EBRD had sufficient funds to support annual investments of €1 billion in the country. Any decision to engage in Egypt would be a complex process. But, Mirow said:

> Twenty years ago, the EBRD rose to the challenge posed by the collapse of communism. Today, in the Middle East, if called upon by our shareholders, we are ready to act, again—championing the values that we hold dear.[17]

Agreement in Brussels

Mirow was in Brussels on 1 March for meetings with the EU's top officials to discuss the EBRD's potential contribution. It was an opportunity to clarify what the different actors could provide by way of support to the new and rapidly evolving developments on the EU's southern borders. The focus was on concrete actions to deliver on Ashton's plea for effective, coordinated assistance.

In parallel to the thinking on the EuroMed idea, work had been going on behind the scenes to update the operational relationship between the EBRD and EIB, led on the EBRD side by Horst Reichenbach, now Vice President Risk and Resources. The impact of the financial crisis and the arrival of the EBRD in Turkey had added momentum to the exercise. An agreed position between the two organisations was reached shortly ahead of the Brussels meetings and allowed the two presidents, Mirow and his EIB counterpart, Philippe Maystadt, to sign a Memorandum of Understanding (MoU) on EIB and EBRD activities outside the EU region. It underscored how they could cooperate more effectively in the relevant countries.

The new framework for cooperation, which was co-signed by European Economic and Monetary Affairs Commissioner Olli Rehn, aimed to:

> Enhance the combined impact of the two banks' operations in the interest of both the beneficiary countries and the banks' shareholders. Strong cooperation and coordination will make the best use of the core competencies and comparative advantages of both organisations.[18]

---

17 EBRD Press release, 23 February, 2011. 'History can often move at breakneck speed'.

18 EBRD Press release, 1 March, 2011. 'European Commission, EIB and EBRD sign Memorandum of Understanding'.

Reporting back to the Board the following day on his meetings with EU Commission President José Manuel Barroso, Ashton, Maystadt, Rehn and Enlargement Commissioner Stefan Fuele, Mirow said there was strong support for the EBRD's involvement in cooperation in North Africa. Maystadt had in particular endorsed the MoU as a basis for the EIB and the EBRD to work together in Egypt, as they were doing already in Turkey.

That day, at a news conference in Brussels, Barroso set out the latest EU position on the North African developments and called for a "new political paradigm" for the EU's Southern Neighbourhood. "We need a 'Pact for Democracy and Shared Prosperity'," he said.

There was no reference to the new Bank for the Mediterranean. The project was eventually dropped. It was clear, especially following the signing of the latest agreement between the EBRD and the EIB, that the two institutions would each make their own contributions to the transformation of the Arab region, while working more closely together.

Barroso spoke of using the leverage of EIB funds to prepare a stimulus package for the region, with a particular focus on SMEs to help create jobs and called on the EBRD to make its contribution:

> I also believe the EBRD can do more, and be more active in the South. All this is the intention of the EBRD if the Member States that are members of this bank are ready to change the statutes. Yesterday I already spoke to the President of the EBRD who would support this change in the statutes of the EBRD so that they can use their great expertise of transition and in financial matters to support the Southern Mediterranean.[19]

Egypt again, and Israel

Aboulnaga, who had retained her position as planning and international cooperation minister following the fall of Mubarak, reaffirmed Egypt's strong commitment to becoming an EBRD recipient country under the new administration. In a letter to Mirow on 10 March, she thanked the

19 'Jose Manuel Durao Barroso President of the European Commission's statement on the situation in North Africa, Press point Brussels,' 2 March 2011, https://ec.europa.eu/commission/presscorner/detail/en/SPEECH_11_137.

President and EBRD management for the decision to accelerate the technical assessment process.

Aboulnaga said the interim government was working intensely on democratic reform as well as social and economic development. On the political front, Egypt was focusing on handing over power to a civilian democratic government through fair and transparent presidential and legislative elections. Social and economic development targets aimed to meet the demands of disadvantaged people, improve living standards, provide affordable housing especially for the youth and to foster job creation through a strong boost for microfinance and SMEs. She explained that the government believed the EBRD's engagement in Egypt was "of the essence".

"I hereby strongly reaffirm our request to become [an EBRD] country of operations," she said, noting that she and the Egyptian Foreign Minister were in contact with G7 authorities with a view to receiving their agreement.[20]

One key non-G7 shareholder that Mirow was eager to bring on board was Israel, whose views were crucial in reaction to developments on its doorstep. He made a trip to Israel for talks in what the *Jerusalem Post* described as an effort to calm Israeli nerves ahead of any possible EBRD investment in the neighbourhood. The *Jerusalem Post* quoted Mirow as saying:

> My own perception is that any effort to support the stabilization of Egypt and to increase the opportunities for young people could be helpful for Israel, too. ... We have not only an economic but a political mandate... Every taxpayer in Israel can be sure our money will not fund authoritarian regimes or corrupt elements in the economy.[21]

Morocco expresses interest in recipient status

In Morocco, popular protests had erupted in February, with thousands taking to the streets to demand constitutional reform and an independent judiciary.

King Mohamed responded in March by announcing plans for a new constitution and calling together political parties, trade unions and civil

20 Letter from Governor for Egypt regarding Egypt's Request for Country of Operational Status, 10 March 2011.

21 Oren Kessler, "EBRD president seeks to calm Israeli nerves," *Jerusalem Post,* 13 March 2011, https://www.jpost.com/international/ebrd-president-seeks-to-calm-israeli-nerves.

society groups to draw up proposals that would be put to a referendum. The monarch's proposals included an independent judiciary, a stronger role for parliament and political parties and a regionalisation programme to devolve more powers to local officials.

The plans were welcomed by foreign powers including the USA, France and the UK, as well as the UN Secretary General Ban Ki-moon who said that what had been seen in the King's speech was a clear indication that he had listened to the voices of his people.

In April, the Moroccan authorities wrote to the EBRD President to express the country's strong interest in becoming a country of operations of the EBRD. The letter from the Minister of Economy and Finance, Salaheddine Mezouar, said:

> We believe that this step would enable the Bank to complement the activities of other international and regional financial institutions to enable Morocco to meet the considerable challenges which it is determined to address.[22]

3. The Extension of the EBRD's Remit

Shareholder backing in Astana

After useful discussions in April among heads of MDBs at the spring meetings of the World Bank and IMF on how they might respond to the situation, management prepared the ground for a decision by shareholders at the Annual Meeting in Astana. The goal was to be able to take clear steps towards an extension of the EBRD's mandate not just to Egypt or Morocco, but across the wider Mediterranean region.

On the eve of the 20–21 May meeting, Mirow got shareholder backing for the plan from a very high source. In a keynote speech on the Middle East on 19 May, President Obama made a specific reference to the EBRD:

> We will work with the allies to refocus the European Bank for Reconstruction and Development so that it provides the same support for democratic

22 Letter to the EBRD President concerning Morocco's interest in becoming a country of operations, 13 April 2011.

transitions and economic modernization in the Middle East and North Africa as it has in Europe.[23]

Encouraged by this and other evidence of momentum building towards a MENA role for the Bank, Mirow laid out a strong case for EBRD intervention in the new region in his opening speech to the Astana meeting, saying:

> Beyond the capacity, resources and expertise, I believe we also have a responsibility. The Romans called the Mediterranean "mare nostrum" and what happens in the region is indeed of fundamental importance for all of us. ... The experience with transition is something that can and should be shared. The people in that region, as in ours, deserve to see their political aspirations matched by palpable economic gains.[24]

Following on from earlier comments by the US President, Washington's Treasury Secretary, Timothy Geithner, set out the basis for the US position as he addressed the Astana audience:

> This year, EBRD Governors have the opportunity to support a historic moment in a region that does not fall within the Bank's geographical scope but does fall squarely within its fundamental mission. ... The EBRD is a powerful tool that we should draw upon.

There was broad, if nuanced, support from the other large shareholders. France described EBRD activity in the region as a "powerful political symbol."

Germany was slightly more guarded, but "willing in principle" to proceed, while insisting that any new EBRD country of operations had indeed to be committed to and applying the principles of democracy and market economy. Japan, too, insisted on the multiparty democracy element.

Italy said there was an historic opportunity to maintain the momentum of change in North Africa. "The EBRD, given its unique expertise in supporting transition through the development of the private sector, should rise to the challenge."

---

23 'Remarks by the President on the Middle East and North Africa', White House Press Office, 19 May 2011, https://obamawhitehouse.archives.gov/the-press-office/2011/05/19/remarks-president-middle-east-and-north-africa.

24 Opening speech to the 20th EBRD Annual Meeting, 20 May 2011.

The United Kingdom strongly supported the extension of the Bank's geographical mandate to North Africa and the Middle East. The UK delegate said: "Events still unfolding in that region are of historic importance, and extending the Bank's work should be part of a positive international response to support the ambitions of the people in these countries."[25]

Canada was supportive while encouraging the Bank to explore ways to follow through on the successes in its current region of operations, especially on pursuing the graduation of more advanced EBRD countries in the European Union.

The EU delegate, noting that the EU had been long supportive of concerted IFI action in countries of the south Mediterranean, welcomed the move saying, "most of these countries face challenges that directly concern the mandate of this Bank", such as the "need to accelerate private sector development." The EIB, however, while acknowledging "recent good examples of cooperation" between the two MDBs in Turkey, took a more cautious line. "The expansion into North Africa will require not just additional consumption of capital but ... perhaps a significant call on the EBRD's management time," said its delegate, adding: "Going beyond North Africa needs further deep analysis and calm reflection."

Russia warned against "precipitate action" and saw serious risks and challenges. "This subject needs to be discussed thoroughly and openly, and it should be linked to the issue of graduation."

The Astana conference ended with an agreement to review expansion into countries along the coastline of the Mediterranean, a region the EBRD would call the southern and eastern Mediterranean (SEMED). The EBRD's Board of Governors tasked the London-based Directors to come up with recommendations on this extension of the geographic mandate.

There were conditions. Any expansion had to ensure that the EBRD would not require additional capital contributions and, just as in the case with the previous expansion to Turkey, that such a move should not compromise the scope and impact of the Bank's operations in the existing recipient countries.

But there was now clear support for yet another EBRD expansion.[26]

---

25 Delegate speeches to the 20th EBRD Annual Meeting.

26 EBRD Press statement, 20 May 2011. 'EBRD shareholders take steps towards supporting emerging Arab democracies'.

The G8 at Deauville

One week after the Astana Annual Meeting, leaders of the Group of Eight (G8) countries met in the northern French resort of Deauville under the French presidency of Sarkozy[27] to discuss their response to the Arab uprising. Just as Baroness Ashton had in February, the G8 evoked memories of the backdrop to the EBRD's creation 20 years earlier. The 26-27 May Deauville Summit Declaration on the Arab Spring opened:

> The changes under way in the Middle East and North Africa (MENA) are historic and have the potential to open the door to the kind of transformation that occurred in Central and Eastern Europe after the fall of the Berlin Wall.
>
> The aspiration of people for freedom, human rights, democracy, job opportunities, empowerment and dignity, has led them to take control of their own destinies in a growing number of countries in the region. It resonates with and reinforces our common values.

The G8 made a specific appeal to the EBRD to join in what was now being dubbed the 'Deauville Partnership'[28] and once again to extend its reach. In any joint action by MDBs, the G8 wanted to "leverage the experience of EBRD in accompanying economic transition". The statement continued:

> We call for an appropriate regional extension of the geographic scope of the EBRD's mandate, in order to support the transition in countries of the region which embrace multiparty democracy, pluralism and market economies.
>
> The EBRD has been a unique instrument to help transform the economies of Central and Eastern European countries engaged in the same

27 France led the G8 and G20 in 2011.

28 The Deauville Partnership began with Egypt and Tunisia and soon included Morocco and Jordan, and later Libya and Yemen. In their Declaration the G8 leaders said: "Today we launched the 'Deauville Partnership' with the people of the region, based on our common goals for the future, in the presence of the Prime Ministers of Egypt and Tunisia, the two countries that originated the movement … We stand ready to extend this long term global Partnership to all countries of the region engaging in a transition towards free, democratic and tolerant societies ('Partnership Countries'), beginning with Egypt and Tunisia, in association with countries wishing to support transition in the region. This Partnership enshrines common values of freedom and democracy …", Munk School, Trinity College, University of Toronto, http://www.g8.utoronto.ca/summit/2011deauville/2011-arabsprings-en.html.

> dynamics, with its focus on private and entrepreneurial initiative. The financial strength of EBRD makes it possible to extend its area of operation consistent with its current strategic commitments, notably in the existing countries of operation.

According to one senior G8 official involved in the preparations for Deauville, it was a time of unprecedented cooperation among leaders, where a coordinated IFI response was supported by a number of Sherpas with strong financial backgrounds and multilateral experience. France had intended to focus on common principles for the internet at Deauville but the challenge of a response to the Arab Spring very quickly took centre stage. Involving the EBRD was particularly attractive, not only because of the historical narrative and its mission to support the private sector—in its way responding to the pleas of the Tunisian street vendor—but it fitted leaders' desire to do something new. And the EBRD could move quickly, unlike any new bank which would take time to set up. It helped too that the EBRD had capital available, which had been boosted only the previous year.

The G8 wanted the EBRD to move swiftly:

> To fast-start EBRD support to and leverage its experience in private sector development and job creation in the region until the ratification of the extension is completed, we will work with the EBRD towards the creation of a dedicated transitional facility, to allow the bank's operations to start as early as possible to the benefit of prospective recipient countries...[29]

The EBRD had established by now that it would be able to make investments of around €2.5 billion a year in North Africa without seeking additional funding from shareholders.

Applications for EBRD membership and a three-stage plan

Following the requests for funding from Egypt and Morocco, other members of the Deauville Partnership also made applications to the EBRD for membership and recipient status.

29 Ibid.

The authorities in Tunisia, where the uprisings around the region had begun, wrote to Mirow in June to say the country was unveiling reforms. The expertise of the EBRD would be "extremely useful in our current circumstances", said Tunisia's Minister for Planning and International Cooperation, Abdelhamid Triki. Tunisia had embarked resolutely on a path of political, economic and social reforms to achieve democratic transition and to meet the aspirations of the Tunisian people, he said. The government's Recovery Plan, which had recently been approved after consultation with civil society, aimed to ensure transparency, good governance, and accelerate growth in order to stimulate social cohesion.[30]

Jordan would follow suit in September, saying the country had sought to accelerate measures to strengthen the country's democratic governance. "The Government believes that the EBRD can play an important role in promoting and sustaining this important process."[31]

The Astana resolution had called on the Directors to come up with proposals for expansion by 31 July. In their report, the Directors recommended a three-phase approach that would allow for a timely start to activities in the region even before securing unanimous agreement from all the shareholders on an extension of the remit.

In a first phase, the EBRD could offer technical assistance and similar activities funded by cooperation funds that could be available as early as the fourth quarter of 2011. Under the second phase, the Bank could provide investments to "potential recipients" financed from a Special Fund. The amendments of the Agreement Establishing the Bank to enable the creation of such a fund would only require the support of two-thirds of the Governors and three-quarters of the total voting power of the members. Full-scale investment, financed from ordinary capital resources, could follow in the third phase after an amendment of Article 1 of the Agreement Establishing the Bank, expanding the geographic scope of the Bank to include the new recipient countries.

The earlier decision on Mongolia[32] offered a useful precedent for the expansion of the Bank's geographic remit. Article 1 had to be amended by adding in the relevant places, alongside Mongolia, "and each of such [member] countries of the Southern and Eastern Mediterranean."

---

30 EBRD Press release, 24 June 2011. 'Tunisia requests membership of EBRD'.

31 EBRD Press release, 21 September 2011. 'Jordan requests membership of EBRD'.

32 See Kilpatrick, *After the Berlin Wall,* pp. 319–322.

Article 18 which deals with Special Funds also had to be amended, to allow for the creation of Special Funds for use in "Potential Recipient Countries" (not just recipient countries).

Finally, Governors were to be asked to confirm an interpretation that cooperation funds could be used in the countries of the region for technical assistance and the preparation of Bank operations, pending the amendments of Articles 1 and 18 of the Agreement Establishing the Bank taking effect.

The report and the three separate resolutions providing for these parallel steps, together with a request that Tunisia be admitted as a member of the EBRD, were sent to Governors on 3 August with a deadline for decision by 30 September 2011.

Regional boundaries

Publication of the report also followed debate about the geographic definition of any expanded area of activity.

Too narrow a regional definition might leave out current or future aspirant democracies and therefore dilute the international community's offer of support for the Arab Spring. But anything too wide might reduce the EBRD's ability to offer meaningful financing.

Directors agreed to propose an extension to the southern and eastern Mediterranean region, "consisting of the countries that have a shoreline on the Mediterranean as well as Jordan which is closely integrated into this region."[33] Use of the acronym SEMED soon became commonplace.

Iraq, which like Jordan does not share a Mediterranean coastline, was not included, despite some pressure from the USA. There had been a suggestion that the definition refer to countries on the Mediterranean, as well as Jordan—"and countries like Jordan." This proposal did not receive support.

The SEMED region now technically covered the four original Deauville Partnership countries, Egypt, Jordan, Morocco and Tunisia, and also Algeria, Libya, Lebanon and Syria, as well as the West Bank and Gaza.

To qualify for full EBRD financing, individual countries would still have to be or become EBRD shareholders and subsequently apply for and be granted recipient status.

---

33 At its closest point, Jordan is about 40 miles from the Mediterranean coast.

The process for the West Bank and Gaza was different because of its particular political status, but there were ways to allow it to become eligible for finance.

Endorsement for EBRD activities

At a G8 finance ministers' meeting in Marseille in September, the leading IFIs and MDBs threw their weight behind the Deauville Partnership. The EBRD took the opportunity to map out the progress it had made in extending its geographic remit and senior representatives from the four regional members of the Deauville Partnership attended the conference.

The IFIs strongly endorsed the economic framework of the partnership that they said was tailored to support the individual country economic programmes. These would be "home-grown" and driven by countries themselves. IFI coordination was also key to the external support. During the conference, the EBRD signed Memorandums of Understanding with the African Development Bank (AfDB) and the Islamic Development Bank (IsDB), outlining how the institutions would cooperate in the region in the future. It was very important that the EBRD be seen as a welcome partner in the region rather than as an intruder or competitor.

In their communique in Marseille, the Deauville Partnership Finance Ministers[34] called upon MDBs and regional development funds to step up support for the partnership countries:

> The enlarged group of international and regional financial institutions supporting the initiative brings the total amount available for Egypt, Tunisia, Morocco and Jordan in 2011-2013 to $38 billion in support of suitable reform efforts, in addition to resources that could be available from the IMF.[35]

A representative from Libya attended the Marseille meeting as an observer. Protests in Libya had begun in February 2011 and developed

34 In Marseille the Deauville Partnership, which focused on an economic pillar at the meeting, was extended to include Kuwait, Qatar, Saudi Arabia, Turkey and the UAE, as well as including the G8 countries and Egypt, Jordan, Morocco, and Tunisia. Nine international and regional financial institutions were also active participants.

35 'Deauville Partnership Finance Ministers' Meeting Communiqué', Marseille, 10 September 2011, https://www.afdb.org/fileadmin/uploads/afdb/Documents/Generic-Documents/DP%20Marseille%20communique%20version%20ENG.pdf. Much of the funding represented financing already earmarked for the region. Planned finance by the EBRD, as a newcomer to the region, was genuinely additional.

into a full-scale armed revolt against Muammar Gaddafi, who had been in power for four decades. Backed by Western and several Arab states, the rebels eventually captured and killed Gaddafi a month later. However, the subsequent civil war put on hold developments on support through the Deauville Partnership.

By October, the EBRD's shareholders had overwhelmingly backed the plans for the three-stage expansion of investment activities into the SEMED region, in what Mirow described as "an impressive vote of confidence in our ability to deliver concrete projects that foster transition and improve people's lives".

The Article 1 decision by Governors still had to be formally ratified by national capitals, in most cases with a requirement of parliamentary approval. This was likely to prove time-consuming in some cases. But the earlier stages of the process could move forward even before ratification. The EBRD expected to provide technical assistance for Egypt, Jordan, Morocco and Tunisia in the following weeks or months in preparation for investment projects there.[36]

By December 2011, donors to the EBRD were making significant contributions to fund these technical cooperation activities. A total of nearly €60 million in grant funding, including financing from the EU, bilateral donors and via an allocation from the EBRD's own net income, had been made available.[37]

The first donor-funded project was for a small local transportation company in Alexandria that helped it expand its services to Cairo and to improve its business model and management.

Early in 2012, Jordan and Tunisia had joined Egypt and Morocco as shareholders, as part of the process of becoming potential and then actual recipients of EBRD investments.

The Bank began to open temporary offices in the region, in anticipation of starting activities.

---

36 EBRD Press release, 5 October 2011. 'EBRD shareholders back expansion to support emerging Arab democracies'.

37 EBRD Press release, 13 December 2011. 'The EBRD starts donor-funded activities in southern and eastern Mediterranean'.

Transition-to-Transition

At this time, the EBRD launched a series of successful conferences in the new region that facilitated an exchange of transition and reform experiences between the Bank's existing countries of operations and countries of the southern and eastern Mediterranean region.

The first of these Transition-to-Transition (T2T) events was held in Cairo on 24 October 2011. Aboulnaga welcomed high-ranking guests from eastern Europe, including Former Czech Prime Minister and serving EBRD Vice President, Jan Fischer, and former Polish Prime Minister, Jan Krzysztof Bielecki, who had been a long-serving Polish Board Director at the EBRD. Neither of the visitors played down the challenges of the transition process.

Fischer, whose country had graduated from the EBRD process four years earlier, said: "After 20 years, my country is still in a transition. The process involves intertwining economic and political issues, legal changes, as well as social aspects." Bielecki told the meeting that transition inevitably brought instability and governments had to find time for strategic thinking.

The sessions had been developed under the leadership of EBRD Chief Economist, Erik Berglof, who stressed the peer-to-peer essence of the conferences that were opportunities for sharing from both sides, allowing all countries to understand the challenges of transition. Similar events were subsequently held in Tunisia and then Morocco and Jordan.

4. Building up Operations

Good governance at the EBRD

The stage was set for an important Annual Meeting in May 2012 in London, where Governors were due to endorse the Bank's moves into SEMED and vote on the EBRD Presidency as Mirow's term of office was due to end that summer.

A new German government, which had come to power after Mirow's appointment in 2008, did not back his re-election for another term, which opened the door for candidates from other countries. Meanwhile, the traditional alternative country to lead the EBRD, France, was consumed by electoral campaigning in the dying days of the Sarkozy Presidency, and the

candidate they had endorsed, de Fontaine Vive, did not gain traction among several shareholders. Eyeing an opportunity, the UK's Chancellor of the Exchequer, George Osborne, lobbied his finance minister counterparts to suggest the election be publicly contested, while also offering the senior UK civil servant Sir Suma Chakrabarti as a well-qualified candidate.

This was a neat ploy. No election for the position as head of an MDB had ever been openly contested. The suggestion that the EBRD do so was not only good governance, but it also had the added bonus that it might first occur in an institution dedicated to upholding democratic principles. The move was made more credible in the circumstances of EBRD expansion into the SEMED region by proposing a candidate who had strong managerial and development experience, rather than a candidate with the more typical long-standing finance or central bank background presented for the position up until then.[38]

Ahead of the meeting other candidates put their names forward, each with a statement of their future vision for the EBRD, including how they might improve the relevance and functioning of the institution. As well as Mirow, now forced to seek re-election, de Fontaine Vive and Chakrabarti, two others applied for the job: Božidar Đelić, Deputy Prime Minister of Serbia, and Bielecki, the former Polish Prime Minister. Sequential knockout voting procedures meant that several rounds of voting took place that weekend, adding to the drama.

The end result was the election of Chakrabarti to replace Mirow. The decision was, among other things, notable for the accession for the very first time of a Briton to the presidency of the EBRD, signalling the end to a tradition—which some believed, harking back to the original negotiations, was an unwritten agreement—where the top position at the EBRD was divided between France and Germany.[39] Two terms later, the EBRD presidency returned to French hands.

---

38 Chakrabarti took a keen interest in development issues having been born in West Bengal and as a previous head of the UK's development ministry, DfID.

39 Such unwritten agreements were not unusual among IFIs, with for example a longstanding arrangement between the USA and Europe over the top positions at the World Bank and IMF. When the EBRD was founded among the compromises made was that the headquarters of the institution would be located in London and its first President would be French (and that the initial First Vice President would be a US citizen). (See Kilpatrick, *After the Berlin Wall*, p. 38.) Practice thereafter was that the presidency alternated between France and Germany, until 2012. (In 2018 the arrival of a German national, Jurgen Rigterink, as First Vice President broke with the tradition of the previous 27 years.)

A €1 billion Special Fund and the first investments

The Bank also announced at the London meeting the approval of the €1 billion Special Fund that would signal the start of its investments in the Arab world.[40]

Those investments started flowing in September, as the Board of Directors signed off the first three projects—but only for Jordan, Morocco and Tunisia. These three countries had requested "potential recipient" status in July and this had been granted in September,[41] opening up the way for projects to be financed from the fund.

The initial projects included a US$ 30 million trade finance line for InvestBank in Jordan to promote lending to small- and medium-sized enterprises. There was a €20 million commitment to a private equity fund sponsored by AfricInvest-TunInvest, one of the leading local private equity firms in Tunisia and Morocco, and a loan and a trade finance facility for Morocco's Société Générale Marocaine de Banques.

Egypt had formally sought potential recipient status shortly after the other three countries and it was granted in November, allowing it to be eligible for investments via the Special Fund. But it proved impossible to seal any investments at that time during a period of continuing political and social uncertainty. Divisions had remained in the country, pitching old guard supporters of Mubarak against the newly-elected, Islamist-backed President Mohamed Morsi amid concern about the persistent role of the military in Egyptian politics.

At his first main press conference after taking office, Chakrabarti addressed this issue head on. He told journalists in October:

> On Egypt, it is very simple. The reason for the delay and the reason why Egypt is now a few weeks behind, if you like, is simply because of the political situation in June, July and August. We did not really have anyone to talk to at the time because the government was being re-formed, as you know. Those initial elections took place and a new government then had to be formed. We did not have a direct interlocutor.[42]

---

40 EBRD Press release, 19 May 2012. 'EBRD shareholders approve fund to start investment in emerging Arab democracies'.

41 Full recipient membership status, which had been requested the previous year by Tunisia and Jordan, would only come for each country once the amendment to Article 1 became effective in each case.

42 EBRD Press statement, 1 October 2012. 'Speech transcript: Suma Chakrabarti at a Press Conference on 1 October 2012 in London'.

The new President said he hoped the first investment in Egypt would come the following month and certainly by the end of the year.

The first Egyptian project did not in fact come until early in 2013. And it would take longer for Egypt to become a full recipient of investments from ordinary EBRD capital than the other SEMED countries.

Morsi's period in power was troubled from the start. Constitutional changes were criticised for putting the President above the rule of law. Violent protests continued. A year after his election, he was removed from power in 2013 in a military takeover driven by the country's Defence Minister, General Abdel Fattah el-Sisi.

A further period of interim government followed, which included a crackdown on members of the Muslim Brotherhood that had supported Morsi. On 9 October 2013, the Obama administration suspended some military aid to Egypt in response to the crackdown.

The political developments in Egypt were not making it easy for the EBRD to carry out the mandate it had received from the international community two years earlier. At the same time, civil society organisations were critical of the Bank's involvement.

But management made clear the EBRD's shareholders wanted it to continue to pursue projects in Egypt that could make a difference to the lives of ordinary people there. In an interview during the Annual Meeting of the World Bank and IMF in Washington in October 2013, Chakrabarti said members were eager for the Bank to continue making investments in Egypt provided they pass "a socioeconomic test". He told *Dow Jones*: "All agree it's the sort of thing we should do. It's not business as usual as if nothing's changed, because clearly our major shareholders are thinking about this issue, but at the same time nor is it 'stop doing what you are doing'."[43]

The subsequent political turmoil delayed Egypt's formal admission as a country of operations. After General Sisi stood for election in 2014, won and was sworn into office on 8 June, there were yet further delays requiring another extension of the deadline. Egypt would only become a full country of operations, with access to the Bank's ordinary capital resources, in November 2015.

The other three Deauville Partnership countries had already become eligible for full-scale investment out of the EBRD's ordinary capital in November 2013.

---

43 'EBRD to Keep Investing in Egypt Despite U.S. Pullback on Aid', *Dow Jones*, 11 March 2013.

Gearing up

Even before the creation of the Special Fund that allowed investment in the region ahead of countries reaching full recipient status, key practical decisions had been taken, including the new appointment of a managing director for the region.

Hildegard Gacek, a German national who had held senior managerial positions in the EBRD in Serbia and Romania, as well as in the Caucasus and Belarus and Moldova, was appointed to the position in April 2012. She was no stranger to the EBRD's newest region, having run operations for the Middle East, West and North Africa department of the German Investment Corporation (DEG) for eight years before joining the EBRD.[44]

Gacek led the operational rollout of the EBRD's activities, initially identifying interim office space, appointing managers to run the operations in relevant cities and negotiating Host Country agreements between the EBRD and the national authorities that allowed the Bank to establish a permanent physical presence.

For Gacek, one very strong aspect of the EBRD's early operations was the flexibility of the Bank's three-phase approach which allowed activities to begin right from the word go. "We moved into interim offices. We started to hire local people and we began operations very quickly," she recalled.[45]

There were, of course, challenges but also opportunities from the fact that the EBRD was a completely new face in the region. "We were a complete unknown but then again we also had no legacy," Gacek said. "We really gave these four countries a lot of attention. Of course, we had to establish ourselves. We were brand new. No one knew who we were. We came demanding very high standards from local staff. In time we became an employer of choice."

Gacek attributes the Bank's success to the EBRD's commitment to the new region right from the start, both by the top management with the support of the Board and through the dedication of the staff.

One of the most important differences between the SEMED region and the countries of the former Soviet Union and their neighbours, where the EBRD had invested for the previous 20 years, was in her view the fact that SEMED countries were already market economies. "We were certainly

---

44 EBRD Press release, 2 April 2012. 'EBRD appoints head of southern and eastern Mediterranean region'.

45 Interview, December 2020.

not here to build market economies," she said. "Our role was to improve or enlarge the private sector and the market economy."

To a large extent, she says, the Bank achieved this by insisting on conditions that were part and parcel of any EBRD project in any country across both the private and public sectors. This meant that the EBRD was able to have a much deeper impact through its projects than private or state investors, whether in terms of procurement in the public sector or by achieving far greater accounting transparency in the small and medium-sized enterprises that received loans either directly or via the banks. "This sort of conditionality was new and initially for us it was a challenge. But it worked. And it worked because we made it clear right from the start that we were not just a lender but a partner."

As the countries across the new region moved towards full recipient status and negotiation of Host Country agreements proceeded, permanent offices were set up. First in Tunisia and then Jordan, both in 2013, then Egypt in 2014 and Morocco in 2015. Gacek had a choice in Egypt of whether to locate the EBRD's office in prestigious, but hugely overcrowded, downtown Cairo in a building with spectacular views of the Nile or in the then relatively embryonic business centre of New Cairo.

She chose New Cairo, partly because the office space provided much better conditions for employees, but primarily because that was where business was headed. "Everyone, all the banks, were moving out to New Cairo. The staff had space, daylight, modern equipment and facilities. New Cairo was going be and became the commercial centre of the city."

Jordan

After the very first operations began in September 2012, one major investment in Jordan aimed to address the country's acute energy shortages with the construction of a power plant located 15 kilometres east of the capital, Amman. The project was approved in October in a country which had seen frequent power blackouts. Gacek said at the time: "We are determined to justify the confidence our shareholders have shown in us by doing our bit to support this region in meeting the urgent challenges it faces."

The investment in Jordan's Manakher power plant was a response to an immediately pressing energy challenge. But the EBRD's long-term aim was to help wean Jordan off its dependence on foreign energy by developing its

own sources of renewable power. At the time, Jordan was importing over 95 per cent of its energy. Gacek highlights the EBRD's work to deliver solar plants in Jordan as a major plank of the Bank's contribution to the country. Over the coming years, sustainable infrastructure would assume the lion's share of the EBRD's portfolio in Jordan.

Morocco

So as to be at the heart of the business world in its countries of operations, the EBRD opened its first and principal office in Morocco in Casablanca, rather than the administrative capital Rabat.

By the time this office opened in April 2015, the EBRD had invested close to €500 million in Morocco. One of the early projects in 2013 was to support access to energy for Moroccans, with financing for a programme of rural electrification. The EBRD's investment helped link up over 1,200 remote villages to the electricity supply.

Later that year, a key EBRD investment in Morocco, according to Gacek, was in support of a debut Eurobond issue from BMCE, one of the country's leading banks. Getting access to the Eurobond market was an important step for Moroccan financial institutions and corporations alike. As an anchor investor, the EBRD was instrumental in contributing to the success of this initial listing.

Tunisia

The EBRD office in Tunisia was opened in Tunis in June 2013. Gacek was back there shortly after the country unveiled its first post-uprising constitution in January 2014 and the subsequent formation of a new government. During the two-day visit in late February, Gacek had an opportunity to meet ministers from the new government for the first time and to reaffirm the EBRD's support for Tunisia's economic development and its transition towards democracy.

The new Tunisian constitution had been widely hailed by the international community as a step forward in strengthening the country's political transition following the ousting of Ben Ali. The EBRD fully shared this view, calling the latest political development a "key milestone for Tunisia as it demonstrates the country's commitment to transition".

Chakrabarti visited Tunisia four months later, reinforcing his support for the EBRD's role in the country. By then, the EBRD had already provided financing worth over €140 million via projects that were designed to further promote the private sector, bolster the banking system and foster foreign trade.

One particular area Gacek highlighted in Tunisia was the EBRD's local currency lending in the country. She signed an agreement in 2016 that allowed Tunisian companies to benefit from a new EBRD local currency lending programme. This gave small firms access to affordable local currency loans and also helped boost the availability of local sources of local currency funding.

Egypt

Further allocations were made to the original €1 billion Special Fund before it was wound up in November 2015 after Egypt became a full country of operations. By the time this step was taken, the EBRD had provided more than €1 billion in financing to Egypt, of which 77 per cent had been to the private sector.

Its first investment in Egypt, in a white goods firm, aimed to support the development of local manufacturing, but also to raise skills levels and provide job opportunities in a country where unemployment was an urgent challenge.[46] Since then it has promoted small- and medium-sized enterprises, improved living standards across communities with higher quality wastewater services and helped tap into renewable energy sources.

The EBRD's first investment in the financial sector was with National Bank of Egypt, the oldest and largest commercial bank in the country. That first deal was a credit line for small- and medium-sized firms, aimed at driving forward economic development, with a clear focus on sustainable job creation. Having established a good working relationship with the National Bank of Egypt, the EBRD was able to go further and launch, with its help, a successful Women in Business (WiB) programme in Egypt that strengthened the role of female entrepreneurs.

46 EBRD Press release, 27 March 2013. 'EBRD invests US$ 24.3 million in Egyptian white goods manufacturer'.

Commensurate with the size of the Egyptian economy, the EBRD's investments in the country grew strongly and quickly. By 2019, Egypt had topped the annual rankings of EBRD annual investments for the second year in a row, after moving narrowly ahead of Turkey. New financing rose to €1.2 billion in 26 projects in 2019, after €1.1 billion in 19 projects the previous year.

West Bank and Gaza

Following a request by the Palestinian Authority in January 2015, supported one month later by a letter from the Central Bank of Israel, the EBRD extended its activities to the West Bank and Gaza in 2017, after a careful assessment was made to be sure the Bank would be able to deliver on its transition mandate there.

While the transition case was strong, there were obvious difficulties in investing in this new territory. It was not a member of the EBRD, nor conceivably a potential member, since it was not a member of the IMF (a requirement under Article 6.1). That precluded the use of the EBRD's ordinary capital resources or special funds for any investment.

Instead, and in order to be able to use its full range of its financial products, the Bank adopted a new financing instrument, a Trust Fund.[47] Under the exceptional circumstances that applied in West Bank and Gaza's case, and having established sufficient compatibility with the EBRD's purpose and functions, as required by Article 57, two Trust Funds were set up in order to finance operations, to last for an initial five-year period. One Fund received an allocation of €30 million from the Shareholder Special Fund (SSF), the EBRD's own fund for supporting projects, and the other was established as a multi-donor fund.

47 Under Article 20.1 (vii) permitting the Bank to fully adopt such rules and regulations as necessary to further its purpose and functions, and Article 29.3 allowing Directors to make general policy decisions. Hitherto, cooperation funds (i.e. donor funds) had been used in the territories of non-members for the purpose of early engagement ahead of membership, while the process towards recipient membership (allowing the use of ordinary capital resources) or potential recipient membership (allowing the use of special funds) was carried out. These funds were approved for use in Kosovo from 1999, then for Mongolia in 2001 and later the first four SEMED countries in 2011. This route was not possible for West Bank and Gaza as membership of the EBRD was not an immediately feasible option. Moreover, the nature of such cooperation funds is restrictive in that the Bank administers them on the behalf of donors and they are not available for loans, equity investments, guarantees or other financing by the EBRD nor are they covered by the Bank's immunities and privileges.

Operations began early in 2018 with the EBRD mainly involved in the provision of support for small businesses in the West Bank areas, including financing for women-led businesses, carrying out its activities from its office in Amman. Continuing divisions within the political leadership of Palestine has had an impact on the scope of EBRD activities, which have so far been focused on the West Bank. By the end of 2020, the EBRD had signed eight projects in the West Bank and Gaza for a total amount of US$ 46 million.

Lebanon

In the same year that it began operations in the West Bank and Gaza, the EBRD also extended its activities into Lebanon.

The Lebanese Finance Minister had written to the EBRD President on 6 July 2015, saying the Bank could play an important role in assisting Lebanon's process of democratic and free market transition. He requested membership with a view to Lebanon gaining recipient country status "as and when appropriate".[48]

Membership was approved in December 2015. But, against a backdrop of renewed political volatility in Lebanon, there was a delay before all the requirements of membership could be fulfilled to give the country shareholder status. Membership thus became effective only on 14 July 2017, with shareholders granting Lebanon recipient country status two months later, on 4 September.

Lebanon needed EBRD support for reforms that could boost economic growth and tackle widening inequality. The economy was under particular pressure from the conflict in neighbouring Syria, which had disrupted trade and tourism. Most specifically, Lebanon was suffering under a huge influx of refugees, an estimated 1.2 million, or about one third of Lebanon's population.[49]

The crisis was putting a major strain on labour markets, public infrastructure and government finances. It was also a threat to social cohesion in a country that was already polarised. Unemployment was a significant challenge, with over 20 per cent of young adults looking for work.

48 Letter to the President from the Minister of Finance of Lebanon, 6 July 2015.

49 According to UNHCR, as at June 2015.

A number of other development banks were already working in Lebanon. The EBRD saw its particular niche—as usual—in supporting private sector competitiveness, promoting sustainable supplies of energy, fostering energy sector reforms and energy efficiency. It also aimed to improve the quality and efficiency of public services and to engage the private sector in public infrastructure.

On 15 March 2018, the EBRD launched its first investment in Lebanon, buying a stake in Bank Audi, with an acquisition of shares listed on the Beirut stock exchange. The transaction aimed to support the Lebanese financial market and help expand and strengthen the broader financial sector.

Chakrabarti was in Beirut to mark this first transaction and for discussions with the authorities. He used the visit to reaffirm the Bank's commitment to addressing the enormous strain on Lebanon's infrastructure caused by the influx of refugees escaping from the civil war in Syria.

As previously in both Jordan and Turkey, the EBRD's response to the refugee crisis had been to help create an environment that would strengthen employment opportunities and improve the delivery of services for the benefit of refugees and the citizens of the host countries.

The EBRD continued to deliver investments in Lebanon, supporting small business via deals with the banking sector and promoting foreign trade. But the situation in the country became increasingly complicated for the Bank amid political divisions and a seriously worsening economic downturn.

Political volatility continued in 2020 and a deadly port explosion in Beirut in August compounded an already devastating economic crisis. The blast killed over 200 people, injured thousands, caused billions of dollars' worth of damage and left some 300,000 people homeless.

The Lebanese pound fell to unprecedented levels against the dollar, eroding the savings of ordinary people, paralysing the banking sector that traditionally had been a locomotive of the wider economy and triggering inflation above 100 per cent. The almost total economic stasis in the country made it difficult for the EBRD to operate normally via its traditional private sector channels.

The Bank continued to support trade, especially imports of essential goods, and looked into ways of becoming involved in rehabilitation of damaged energy infrastructure. But key to its involvement was the restoration of

a stable government capable of reaching an accord with the IMF that could unlock the reforms needed to facilitate EBRD intervention.

Iraq

The EBRD's shareholders agreed to Iraq becoming a member of the Bank during the 2020 Annual Meeting, held in virtual session because of the Covid-19 pandemic. Baghdad had applied for membership in 2018, making clear it believed the experience of the EBRD could be applied to supporting Iraq address a number of different challenges.

As a shareholder, Iraq could subsequently make an application to change its status to become a recipient country. This request would be addressed by shareholders in a separate process but would involve a further amendment to the Agreement Establishing the Bank, as Iraq does not lie within the SEMED region.

The EBRD's 2021-2025 strategy included a possible expansion of activities into Iraq within the scope of a wider potential extension of the Bank's remit into sub-Saharan Africa. Shareholders were expected to review any such move in 2022, based on guidance from the 2021 Annual Meeting.

Other SEMED countries

Libya had first been accepted as a shareholder as early as 2014 after an application the previous year. But membership was not immediately formalised given continued political uncertainty in the country. Only in July 2019, did Libya officially become the EBRD's 71st shareholder.

Algeria's request for membership was approved in 2020 and it has requested recipient status. The latest EBRD strategy said progress on Algeria's request to become a country of operations was likely early in the 2021-2025 period.

Of these MENA countries with a Mediterranean coastline, only Syria, where civil war has raged since 2011, has not yet applied for membership.

According to the strategy, political and security uncertainty in Libya and Syria make it highly unlikely they would be granted country of operations status before 2025, "though conditions in Libya may be conducive earlier". The EBRD could however respond positively if the situation changed in either country.

Additional regional offices

In line with the EBRD's increasing efforts to reach out to the more remote areas of the economies where it works, as part of its 'inclusion' agenda which accelerated with the Bank's arrival in the region, it opened other regional offices. In Morocco, offices were established in both Casablanca and Tangiers and most recently in Agadir, while in Tunisia there are offices in Tunis and also in the south-eastern coastal city of Sfax. The EBRD also widened its reach within Egypt, opening an office in the Mediterranean port city of Alexandria in 2017, where the primary focus is on supporting the development of small firms.

5. Ten Years After

An 'on the ground' perspective

Heike Harmgart was the economist for SEMED during the very early days of the EBRD's engagement in the region. She headed the EBRD's first operations in Jordan, from where she later managed the Bank's activities in the West Bank and Gaza and Lebanon and subsequently became Managing Director for SEMED.

Reflecting on the EBRD's contribution, Harmgart said its real impact was made not just in financing individual projects but rather in the combination of investment and engagement with the authorities.[50]

The EBRD had fielded a strong mix of people that was capable of delivering solutions to complex developmental challenges. Local experts with a real understanding of the domestic markets worked hand-in-hand with highly technical teams with experience built up over many years in a winning combination that left a lasting positive impact across the private and public sectors alike. Harmgart said:

> We did not just help finance a solar plant. We worked with the authorities on the development of the tariff systems that were need for solar energy across the country. Once the solar or wind power was becoming available, we worked on how it was linked up with the national electricity grid.

50 Interview, December 2020.

That was notably the case in perhaps one of the most visible EBRD projects across the southern and eastern Mediterranean: financing for Egypt's Benban solar power park, the largest solar facility on the African continent.

Before the agreement on the Benban transaction, the EBRD worked for three years with the Egyptian authorities on creating the regulatory conditions for the development of solar power, providing policy advice and technical assistance that was as crucial as the funding itself.

By the same token, the EBRD's support for tourism in resorts like Aqaba in Jordan was about much more than helping to build hotels. The Bank had used its projects to raise skill levels and training opportunities, often for young people for whom unemployment was a major problem.

Its work on cities helped improve the quality of services for the citizens of the region, while also supporting the local authorities' ability to cope with the complex demands of urban financial management.

Some three-quarters of the EBRD's investment had been in the private sector in Egypt. The remaining financing to the public sector had been money well spent. Harmgart recalled with particular satisfaction a project in Egypt, working with a local NGO and the national railway company, on a campaign to improve safety for women when travelling on trains. Without the Bank's involvement, it would have been much harder to get this programme off the ground.

Post-revolution: challenges remain

Ten years after the eruption of popular protest across the Arab world, the EBRD had invested over €13 billion in the southern and eastern Mediterranean, putting a particular emphasis on inclusive sustainable development.

The 10th anniversary in December 2020 of the day Mohamed Bouazizi set himself alight was an opportunity for reflection on developments in the region since then. Some unsavoury leaders had been toppled. Clearly many political expectations remained unfulfilled. There was no quick path to democracy. Parts of the region remain wracked by violence.

The EBRD will continue to debate internally and with its shareholders its relationship with governments where the commitment to, and certainly the application of, democratic values is lagging or has suffered reversals.

Shortly after her election as the EBRD's seventh President in October 2020, replacing Suma Chakrabarti, Odile Renaud-Basso said she believed

the Bank's focus on private sector lending helped strengthen civil society against repressive regimes. "If you cut off all financing I'm not sure that you will support the evolution of the country—and the democratic evolution of the country," the former head of the French Treasury and first female head of any MDB told the *Financial Times* in response to a question about Egypt. The Bank, she said, wanted to "help countries move in the right direction".[51]

A decade on, there is no denying that hopes for the transition of the EBRD's new region have waned. The political challenges and realities of development post-revolution in many respects echo the problems encountered in dealing with the aftermath of the Eastern Bloc.

Yet the EBRD's drive for transforming economies for the better persists in this new geography. As in the early 1990s, the Bank has new and enthusiastic staff from the region who see its potential and want to make a difference. With its investment capacity and mandate for transition towards democratic and sustainable market norms, and with a proven business model, the EBRD remains an IFI of choice for the purpose—just as the G8 at Deauville, and other EBRD shareholders soon after, intended 10 years earlier.

Table 3.1 Gross Domestic Product of countries in the SEMED region, 2019

	GDP per capita, 2019
	Current $, PPP
Egypt	12,284
Jordan	10,517
Lebanon	15,196
Morocco	7,826
Tunisia	11,232
West Bank and Gaza	6,495

Source: EBRD

51 Ben Hall and Sam Fleming, 'EBRD chief defends lending strategy in autocratic countries', *The Financial Times*, 7 December 2020, https://www.ft.com/content/87521b23-234a-4efd-9584-82e8f18f4de5.

Table 3.2

EBRD's Annual Bank Investment (ABI) in countries of the SEMED region, by share of portfolio, 2019

€ million	ABI - Reported Rates	Portfolio (EBRD)	% of Portfolio
Egypt	1,047	4,423	54
Jordan	73	1,016	12
Lebanon	28	242	3
Morocco	742	1,653	20
Tunisia	242	831	10
Total	2,131	8,166	100
West Bank & Gaza	30		

Source: EBRD

Chapter 4
Operations in Greece and Cyprus

Introduction

In 2010, as the EBRD regions slowly appeared to be pulling out of the worst downswing since the collapse of communism, another threat was looming that would put emerging Europe's recovery back on hold.

Just like the crisis that erupted in 2008, which was an import from the more advanced west triggered by problems in the US mortgage market, so the new threat came from the countries of the eurozone: western European nations using the euro as their common currency.

A debt crisis was emerging that would engulf Cyprus, Greece, Ireland, Italy, Portugal, and Spain. It would fundamentally divide the currency bloc, pitting the eurozone's periphery against its more fiscally rigorous core, which included nations like Germany and the Netherlands.

Tensions within the zone escalated and for some time threatened to blow the whole currency system apart, barely more than a decade after it had come into existence. As the closest and largest export market for many EBRD countries of operations, the threat of a break-up of the eurozone was unwelcome news so soon after the previous global shock.

One unexpected outcome arising from the eurozone turmoil was that Greece and Cyprus—both eurozone members and founding shareholders of the Bank—would become countries where the EBRD was also an investor.

Governors agreed at the EBRD's Annual Meeting in May 2014 in Warsaw for Cyprus to become a temporary recipient of EBRD funding, under the condition that there would be no more financing beyond the end of 2020. In November 2020, the Bank duly announced that investments would end.

Greece switched its status in 2015, one year after Cyprus, also signing up for a temporary, five-year period during which it would be an EBRD country of operations.

In the case of Greece, however, shareholders extended the five-year period until the end of 2025, at the request of the Greek authorities.

This was yet another departure for the EBRD, away from its original focus on the eastern European countries that rose from the rubble of communist collapse at the start of the 1990s.

The extension of the remit to Turkey and then to the southern and eastern Mediterranean region had placed the Bank in a very different geography and cultural hinterland from the post-communist eastern European states.

But the additions so far to the EBRD's countries of operations were still very definitely emerging or developing economies. Turkey's per capita GDP in 2010 for example was about US$ 10,750, and it was less than one-half this amount in the southern and eastern Mediterranean (SEMED) region countries.[1]

The move to Cyprus and Greece was a completely different proposition. GDP per capita was over US$ 31,000 in Cyprus and close to US$ 26,900 in Greece, more than ten times higher than in Egypt. Nor was the EBRD investing as it had done in, say, Poland or Hungary—richer countries that were preparing for membership of the European Union.

Cyprus and Greece were not only members of the EU but also part of the eurozone; in Greece's case, already for well over a decade by the time the EBRD started to invest.

There were nonetheless good reasons to lend a helping hand at a time when these two countries each faced separate but grave crises of their own in the early part of the new decade. As with other EBRD recipient countries' experiences during the global financial crisis, their lack of resilience became all the more obvious once the veneer of growth fell away and output collapsed to reveal large structural weaknesses.

---

1 World Bank figures report GDP per capita in 2010 in Egypt, Morocco, Jordan, and Tunisia as US$ 2,650, US$ 2,850, US$ 3,750 and US$ 4,150, respectively.

1. Greece and the Eurozone

How well-prepared Greece was for membership of the eurozone remains a subject for discussion. To a lesser extent, similar questions could be asked of Cyprus. What was certainly clear many years after their accession to both the EU and the eurozone was that both countries faced significant structural challenges.

Greece became the 10th member of the European Community in 1981, seven years after democracy had been restored to the country in 1974 with the overthrow of a military regime. It was not among the first group of 11 countries that formed the eurozone in 1999, but signed up two years later at the start of 2001.

In 2004, however, the Greek authorities admitted that Greece had joined the eurozone on the basis of figures that understated the true level of its fiscal deficit. One of the three Maastricht tests for eurozone membership—covering levels of inflation, as well as debt and deficit levels—was that the government deficit had to be below 3 per cent of GDP.

In November 2004, the government conceded that Greece's budget deficit had not been below 3 per cent since 1999. This was an embarrassment for Greece and for the eurozone, even though Greece escaped any sanctions for failing to keep to the Maastricht criteria. After all, just one year earlier, the EU powerhouses France and Germany had also exceeded their deficit limits.

However, it was this very year, 2004, that eight former communist countries—all recipients of EBRD financing—had joined the EU. The EU8—Hungary, Poland, the Czech Republic, the Slovak Republic, Slovenia, Estonia, Latvia and Lithuania—had faced tough choices and made often painful policy decisions to bring their economies into shape for EU membership. They were frequently on the receiving end of pious sermons about the need for even more fiscal rigour as they set their sights on the next goal of joining the euro.

As economics commentator Katinka Barysch was quoted as saying at the time, the EU risked being accused of double standards as long as the European Central Bank (ECB) carried on telling the east Europeans that they had to stick strictly to the 3 per cent rule to get into the euro. "These countries will say the ECB wants them to be holier than the Pope," Barysch said.[2]

---

2 'Greece admits fudging euro entry', *BBC News,* 15 November 2004, http://news.bbc.co.uk/1/hi/business/4012869.stm.

Despite Greece's violation of the Maastricht criteria, fiscal profligacy continued and the government deficit and public debt levels grew larger.

By late 2009, the debt to GDP ratio was almost double the 60 per cent level advised under EU rules. Early the following year, when Greece was upbraided in an EU report for "severe irregularities" in its accounting procedures, the deficit for 2009 was announced to have reached 13.6 per cent of GDP, more than four times the maximum set in the protocol to the Maastricht Treaty.[3]

By now the ECB was having to deny reports that Greece would be asked to leave the eurozone; and austerity plans were being met with demonstrations and riots on the streets of Athens. Greece, and the eurozone, were in a deep crisis.

Cyprus

The other two countries that joined the EU on 1 May 2004 were Cyprus and Malta, another founding member of the EBRD. Both countries adopted the euro in 2008.

The seeds of the financial difficulties that were later to engulf Cyprus were sown in those four years between EU and eurozone membership. During that period, growth was strong, averaging almost 5 per cent a year, but little or no attempt was made to address pressing challenges or key structural issues on the divided island. There was for example no progress in the privatisation and modernisation of public services and infrastructure.

Among the problems that would loom large just a few years later, and where the EBRD would play its most important role, were the inadequate standards of governance and supervision in the financial sector. The banking sector was bloated, with assets equivalent to eight times GDP.

There was huge exposure to Greece, with loans outstanding to Greek residents equivalent to 130 per cent of Cyprus's GDP by 2008, and bank holdings of Greek government bonds as high as 30 per cent of GDP.

The economy's boom in these four years was based on high private consumption, rapid credit growth (and an associated housing bubble), and a current account deficit financed to a large and precarious extent by non-resident financial flows into the country, primarily from Russia, attracted by a low corporate tax regime and beneficial offshore euro deposit arrangements.

---

3 'Timeline: The unfolding eurozone crisis', *BBC News*, 13 June 2012, https://www.bbc.co.uk/news/business-13856580.

A heavy dependence on non-domestic financial services and the financial inflows meant the moment that the financial system globally went into a nosedive in the last quarter of 2008 there was nowhere else for Cyprus to turn. Its economy fell back swiftly the following year as its main banks took the brunt of the fall.

2. Impact of the Crisis

The turbulence in Cyprus and Greece had far-reaching consequences for both countries. The Cypriot banking sector would emerge radically changed. Greece suffered a recession of devastating proportions.

A survey conducted by the EBRD in collaboration with the World Bank in 2016 revealed that the Greek economic crisis had inflicted greater pain on ordinary people than the global financial crisis had earlier unleashed on the people of eastern Europe. Between 2008 and 2015, the Greek economy shrank by more than one-quarter. Unemployment jumped by over 17 percentage points with youth unemployment running at a staggering rate of over 50 per cent between 2012 and 2014.

Behind the figures lay an even grimmer story revealed by the *Life in Transition Survey III.* According to that poll of citizens, 92 per cent of Greek respondents said the crisis had affected them "a fair amount" or "a lot".[4] Some 76 per cent of respondents experienced a negative income shock, such as reduced wages or pensions, job losses, delayed or suspended wages and decreased working hours between 2010 and 2016. That compared with one in two households in the transition region and about one in three in western Europe between 2008 and 2010. Almost 44 per cent of Greek households saw their wages or pensions reduced between 2010 and 2016.

Cyprus fared better but its GDP also dropped significantly—by more than 11 per cent between 2011 and 2014. Much like a resource-rich country facing a significant commodity price fall, Cyprus's ability to repair the damage—in this case to its financial sector—was heavily constrained (its two largest banks were insolvent), and it would take time to rebuild confidence and alternative sources of income.

---

4 *Life in Transition III*, Chapter 4, EBRD, 2016, https://litsonline-ebrd.com/.

3. Problems in South-eastern Europe

Back in 2010, the problems within the eurozone were initially just a shadow hanging over what looked like a genuine bounce back in central and eastern Europe from the deepest recession in the region since the start of the transition period. Two years after the Lehman Brothers shock, things were slowly starting to look up for the region.

In an outlook published in late October 2010, the EBRD's economists said emerging Europe was gradually experiencing a more broadly-based economic recovery. There were country variations, but the region as a whole was expected to expand by over 4 per cent in both 2010 and 2011, compared with the contraction of 5½ per cent in 2009.

Countries like Russia and Kazakhstan were doing particularly well, supported by higher oil prices, large-scale fiscal stimulus packages and banking system support. Economies in eastern Europe and the Caucasus were also benefiting from higher commodity prices, as well as a revival in remittance flows, while central Europe and the Baltics were seeing an upturn on the back of a stronger than expected recovery in western Europe.

The residual problem area was south-eastern Europe, which was expected to see another contraction in 2010. One particular threat to this sub-region was the continuing crisis in Greece where the earlier boom, predicated on low interest rates, was imploding.

Greek government bond yields were rising and would peak at around 30 per cent in 2012.

The risks to south-eastern Europe of a major spillover from Greece had been contained so far, said the economists, but warned that it still had the potential to disrupt economic activity in the region if the situation deteriorated.[5]

Support for Greek bank subsidiaries

Greek banks were heavily engaged in countries like Albania, Bulgaria, Romania, and Serbia. Under the Vienna Initiative, the EBRD had already stepped in to support the subsidiaries of western banks headquartered in countries such as France, Italy and Austria but active in its region.

5 'EBRD ups emerging Europe GDP outlook', *Reuters*, 28 October 2010, https://uk.reuters.com/article/ebrd-gdp/update-1-ebrd-ups-emerging-europe-gdp-outlook-idINLDE69R1GD20101028.

In the latter part of 2010, the EBRD turned its attention to the subsidiaries in the Balkans of the troubled Greek banking sector. In October, it announced a package worth €630 million that was channelled through subsidiaries of Eurobank EFG in Bulgaria and Serbia, of Alpha Bank in Romania and Serbia and of Piraeus Bank in Albania, Bulgaria and Romania.

The package for these private Greek bank subsidiaries was topped up to a total €980 million two months later, with €350 million for the banking units in Bulgaria, Romania and Serbia of National Bank of Greece. The total financing package was divided into two equal tranches, with €490 million disbursed at this stage.

The EBRD's activities at this time were aimed primarily at supporting the economies of its existing countries of operations in south-eastern Europe, bolstering banking units that were of systemic importance in Albania, Bulgaria, Romania and Serbia.

It was only after the crisis deepened significantly further in Greece and Cyprus that the possibility of EBRD investment in the two countries, and in particular the financial sector, become a reality. The final step came after much more discussion and, in the case of Greece, a series of interim stages.

The Greek economy slid further into crisis in 2010, suffering under the weight of market concerns about excessive government debt as a result of the under-pricing of risk following the country's adoption of the euro.

In Cyprus, a deep economic recession had been triggered by a banking crisis so severe that it saw the complete disappearance of the country's second largest bank and a €10 billion rescue package in May 2013 by the European Commission, the IMF and the ECB, collectively known as the Troika.[6] The EBRD's financial institutions and restructuring expertise was the primary reason behind the start of the Bank operations on the island.

4. Greece Turns to the EBRD

Until the crisis, Greece had been like any other non-recipient shareholder country. There was, however, very active cooperation between Greek banks and corporates and the EBRD in the Bank's countries of operations.

---

6 IMF Press release, 15 May 2013. 'IMF Executive Board Approves €1 Billion Arrangement Under Extended Fund Facility for Cyprus,' https://www.imf.org/en/News/Articles/2015/09/14/01/49/pr13175.

Before the crisis, there was significant liquidity in the Greek economy and companies were expanding into the Balkans. The EBRD was a natural partner. Up until Greece switched to become a recipient country, Greek firms and the EBRD had teamed up for projects worth over €2.3 billion.

Greece was an important source of foreign direct investment in the Bank's regions. The bulk of the joint EBRD-Greek financing had gone to Albania, Bulgaria and Romania. Around one-third of the investment had been in the financial sector.

The nature of the relationship with Greece was to change, however, shortly after Chakrabarti was elected president of the EBRD in May 2012 and assumed office in July. One month into his presidency, Chakrabarti received a letter from the Greek Governor of the Bank, Development Minister Kostas Hatzidakis.

The letter raised the question of whether the EBRD's expertise could be applied in support of an extensive Greek economic adjustment programme.

Greece's policies for restructuring its business sector had many complementarities with the EBRD's activities and expertise, but the minister was not seeking direct investment from the EBRD in Greece: "I would like to invite you to consider the possibility of mutual collaboration on these issues, with a component of technical assistance involvement paid for by European funds, as the first phase of our joint efforts."[7]

The government's priorities for cooperation with the EBRD were business development and trade facilitation instruments for the export-oriented activities of the Greek business sector and helping to promote Greece as a transportation hub.

In his reply to the minister, Chakrabarti said: "The EBRD will work with the Greek authorities, the European Commission and other IFIs to try and define if and how we can help."

Proposals for possible support for Greece were presented to the Board at a meeting in September. They were clear that some strict principles had to be applied. There would be no use of EBRD funds and the process would depend on existing EBRD expertise and resources. In any such move, the EBRD would work in close cooperation with other IFIs and the European Union.

The EBRD could continue to help Greece indirectly by supporting Greek firms in their investments in EBRD regions, building on the long

7 Letter from the Governor for Greece to the EBRD President, 2 August 2012.

experience it already had in financing projects with Greek sponsors in its countries of operations, especially in the Balkans.

As far as delivering finance from other sources to fund technical assistance projects was concerned, there were precedents for using non-EBRD funding for EBRD activities in countries where direct investment was not an option. The Board of Directors could apply an interpretation of the Articles that had been used first in Kosovo and then in Mongolia and the southern and eastern Mediterranean countries before they received country of operations status.

Any deployment of such funds in this way, however, would have to be "broadly compatible" with the purposes and functions of the Bank and "exceptional circumstances" had to exist to support such activity. A background paper suggested that these conditions could be met because: "The economies of a number of recipient countries that neighbour Greece would benefit from any improvement in that country, particularly in relation to inter-regional trade and cross border investment." [8]

Following the meeting with the Board that September, the EBRD engaged with the Greek authorities, local corporates and banks, and the EU institutions to determine the feasibility of putting together a technical assistance programme. It was especially helpful that a former Secretary General and Vice President of the EBRD had been appointed by the European Commission to head the Task Force for Greece and was coordinating technical assistance to support the Greek adjustment programme.[9] Horst Reichenbach was uniquely well-placed to know how valuable deployment of EBRD expertise would be in the difficult circumstances of reforming Greece's economic structures.

5. An Action Plan for South-eastern Europe

Chakrabarti went public on Greece in the first media interview of his EBRD Presidency, telling British newspaper *The Times* that the EBRD would send its own Task Force to Greece to offer advice on boosting private sector growth.

8 Background paper for Executive Session, 4 September 2012.

9 EC President Barroso launched a Task Force for Greece in July 2011 to help Greece design and mobilise technical assistance for the EU/IMF adjustment programme, structural reforms and faster absorption of EU structural funds.

The new President also used that interview to raise an issue that was a particular concern for him and the Bank—the impact of the broader eurozone crisis on other large parts of the EBRD's regions—especially in south-eastern Europe. It would become increasingly clear that the plans for enhanced cooperation with Greece would be placed in the context of the support needed by other EBRD countries of operations. In his interview, Chakrabarti said:

> People talk a lot about Spain, Portugal, Italy and Greece, but not about the impact of the eurozone crisis on eastern Europe and south-eastern Europe, in particular. ... The impact of that crisis on the region is something I feel has been rather neglected in the global debate. The numbers are pretty frightening actually this year and next year in growth terms ...[10]

Chakrabarti pushed hard to put a response to the knock-on effects of the eurozone crisis on south-eastern Europe on the agenda for the meeting of the heads of international financial organisations. Ahead of the Annual Meeting of the IMF and World Bank, held that year in October in Tokyo, *The Times* wrote that Chakrabarti would:

> ... hold discussions with other development banks over a so-called south east Europe recovery plan. The hope is to spearhead co-ordinated provision of debt and equity for banks and other companies in the recession blighted region, while readying help for struggling governments.[11]

Erik Berglof, the EBRD's Chief Economist, was quoted in the same article as saying:

> The south east Europe recovery plan will be a major coordinated effort to help the countries that are most acutely exposed to the spill overs from Greece and the eurozone. Many are in dire straits.[12]

---

10 Sam Fleming, 'Neglected Eastern Bloc feels the chill as lenders retreat', *The Times*, 11 September 2012, https://www.thetimes.co.uk/article/neglected-eastern-bloc-feels-the-chill-as-lenders-retreat-zzllpslk207.

11 Sam Fleming, 'Financial big guns to support Europe's exposed south east', *The Times*, 12 October 2012, https://www.thetimes.co.uk/article/financial-big-guns-to-support-europes-exposed-south-east-gntj5cdj82v.

12 Sam Fleming, 'Financial big guns to support Europe's exposed south east'.

Those October 2012 discussions in Tokyo resulted very quickly in the launch of a new recovery and growth plan by the EBRD, the World Bank and the EIB covering both south-eastern Europe and central Europe, with the inclusion of the latter region coming at the behest of the EIB.

In their joint statement, the three institutions said the new Joint IFI Action Plan for Growth, developed within the context of the Vienna Initiative, responded to the continuing impact of eurozone problems on the economies of emerging Europe. It promised €30 billion of joint commitments would be made during 2013 and 2014. It aimed to rekindle growth in the region by supporting private and public sector initiatives, including infrastructure, corporate investment and the financial sector and was modelled on the successful earlier plan that supported central European economies affected by a liquidity crisis in the financial and corporate sector in the 2008–9 period.[13]

The East Europe editor of the *Financial Times*, Neil Buckley, saw the launch as a feather in the cap for the new EBRD President, writing later that autumn:

> The programme marks a considerable diplomatic success for Sir Suma Chakrabarti, new British president of the EBRD, who has lobbied for co-ordinated action to support south-east Europe, in particular, since taking up the job in the summer.
>
> But what just weeks ago was envisaged as an €8bn plan to support Balkan states hardest-hit by the eurozone slowdown and problems in Greek banks has mushroomed into a programme with far greater financial and geographical scope. It is understood that the EIB, the EU's development bank, insisted the plan be broadened to include central European countries, but in return pledged a significant increase in the financial firepower.[14]

The *Financial Times* quoted Chakrabarti as underscoring once again that some of the problems that emerging Europe was now facing were being imported from the advanced west, making the case for external support even more critical,

13 See Chapter 2. EBRD Press release, 8 November 2012. 'New Joint IFI Action Plan for Growth in Central and South Eastern Europe'.

14 Neil Buckley, 'Banks launch "action plan" for E Europe', 8 November 2012, *Financial Times,* https://www.ft.com/content/a3a35110-29cc-11e2-9a46-00144feabdc0.

> While the world's eyes are fixed on the problems in western Europe, the legitimate requirements of emerging Europe, which has staked so much in the name of economic and financial integration, must not be neglected. The EU's new as well as its aspiring member states, especially in southern and eastern Europe, are once again suffering from problems that are largely not of their making.[15]

6. Small Steps Towards Operations in Greece

When the EBRD Greece Task Force reported back to the Board in November 2012, the proposals for enhanced cooperation were put firmly in the context of the new Action Plan for South-eastern Europe that Chakrabarti had successfully pushed for at the IMF and World Bank Annual Meetings.

Management outlined the plans for continued support to Greek banks and corporates in existing countries of operations, support for cross-border infrastructure and energy investment and for trade finance.

The Task Force confirmed that the Greek economy was operating under severe credit constraints and identified the lack of trade finance as an existential problem for the Greek economy. It also envisaged potential EBRD participation as an observer in a planned Greek Institution for Growth that would lend and provide equity to Greek companies with growth and export potential but which had lost access to capital. There was continued discussion about EBRD technical assistance funded primarily by the EU.

In the discussion with the Board, management made clear that any enhanced cooperation was an integral part of the EBRD's scaled-up support for the countries in south-eastern Europe that were most directly affected by the crisis in the eurozone, and specifically by Greece.

The proposals for support and other forms of technical assistance were consistent with and complemented the new Joint IFI Action Plan for Growth in Central and South Eastern Europe, precisely because the crisis in Greece was one of the main sources of risk in the region. Action taken in support of Greece could make a significant contribution to the stability of south-eastern Europe.

---

15 Buckley, 'Banks launch "action plan" for E Europe'.

Throughout 2013, the EBRD did indeed spend time assessing the situation in Greece and the possibilities of deeper cooperation. There was extensive consultation and information sharing with industry associations and Greek banks. And it was essentially during this period that the Bank and the Greek authorities sowed the seeds for the steps that were to be taken later and which would develop into Greece becoming a recipient EBRD country.

In terms of substance, however, not that much actually happened in 2013, partly because of a growing caution on the part of the Board and an increased degree of risk aversion on the part of management. Very few projects, either in the banking or corporate sectors, were taken forward.

The second tranche of the €980 million credit facility for the 11 subsidiaries of Greek banks in the Balkans had been put on hold after the escalation of the Greek sovereign crisis in the summer of 2011. In 2013, a decision was taken that it would not be allocated, though the Board did agree new trade finance limits for eight of these Greek bank subsidiaries and some energy efficiency projects, as well as cross-currency swap lines for subsidiaries in Serbia and Romania.

A number of corporate projects were deemed too risky and there was very little opportunity for EU-funded technical assistance activities, especially as the EU had its own Task Force in Greece, which left little space for the Bank.

The next key development came during a visit by the EBRD President to Greece and Cyprus in December 2013. Meetings were held on the fringes of a workshop on the future of the banking sector in the Balkans, jointly organised by the EBRD and the Bank of Greece.

In Athens, Chakrabarti and Development Minister Hatzidakis assessed the situation again and discussed possible ways forward. Hatzidakis publicly thanked Chakrabarti for the "major help" the Greek economy was receiving from this funding of the operations of Greek firms elsewhere in south-eastern Europe. Statements were made about funding energy projects in the Balkans, including the Trans Adriatic Pipeline, a gas interconnector between Greece and Bulgaria, and continued funding for Greek companies active in the Balkans.[16]

There was, in public at least, no suggestion of formalising the arrangement by turning Greece into an EBRD country of operations.

---

16 'Development minister meets with EBRD President over Balkan funding', Athens News Agency, 13 December 2013.

7. Cyprus Obtains Recipient Status

During the same trip to the region, Chakrabarti met the Cypriot authorities on 16 December. They did ask about becoming a recipient country.

The Cypriot Finance Minister, Harris Georgiades, followed up the visit with a letter to the EBRD President two days later, where he expressed interest in Cyprus becoming a country of operations "for a limited period". Georgiades said the financial crisis had brought to the surface certain fundamental structural deficiencies in the Cypriot economy. There was a very specific need to restructure and recapitalise the banking sector and for privatisation in such areas as telecoms, power and energy, and sea ports. He believed the EBRD could make very specific contributions with its transition mandate.[17]

EBRD staff visited Nicosia from 16 to 18 January 2014 and reported back to the Board on the challenges that Cyprus was facing, again placing an important priority on restoring the financial sector to good health. Additional areas of potential EBRD involvement lay in the delivery of privatisations, restructuring and regulatory improvements in the energy sector, enabling diversification of energy sources and promoting high-quality investments in selected strategic areas such as tourism.

The next letter from Georgiades to the President, dated 6 February 2014, formally requested that Cyprus become a recipient country of the Bank.[18]

The Board of Directors was broadly supportive but insistent especially on two issues. First, the temporary nature of any engagement in Cyprus had to be made clear. Equally, in taking this step the EBRD had to underscore the very specific nature of the crisis in Cyprus. This was not to set a precedent for any more countries, they implied.

There was however sufficiently broad support for the proposal to be transferred to Governors for their approval at the 2014 Annual Meeting in Warsaw in May.

Another key element in the EBRD's potential engagement with Cyprus was that while the request had come from the authorities in Nicosia, the Bank undertook to conduct its activities across the whole of the de facto divided island, including the northern region, recognised only by Turkey.

17 Letter to the President from the Minister of Finance for Cyprus, 18 December 2013.
18 Letter to the President from the Minister of Finance for Cyprus, 6 February 2014.

The EBRD's work would aim to benefit both the Greek and Turkish Cypriot communities.

The intervention by the Bank came during a rare moment of optimism about a resolution of the bitter stalemate that had divided the island and its people since 1974. Numerous initiatives to bring the two sides together had been tried and failed.

On 11 February 2014, there was an apparent breakthrough, with the publication of a joint declaration from both the Greek and Turkish Cypriot leaders expressing their determination to resume structured negotiations in a results-oriented manner. The status quo was unacceptable and its prolongation would have negative consequences for Greek Cypriots and Turkish Cypriots. Their statement said:

> The leaders affirmed that a settlement would have a positive impact on the entire region, while first and foremost benefiting Turkish Cypriots and Greek Cypriots, respecting democratic principles, human rights and fundamental freedoms, as well as each other's distinct identity and integrity and ensuring their common future in a united Cyprus within the European Union.[19]

However, hopes for a political rapprochement were dealt a heavy blow just eight months later when talks were halted after Turkey sent a ship to monitor an oil and gas exploration mission off the southern coast of the island, reflecting the strong opposition by Turkish and Turkish Cypriot representatives about moves by the Government of the Republic of Cyprus to explore hydrocarbon resources around the island.

The EBRD continued to emphasise its support for the whole country and its two communities, as well as its expectations that political unification could be achieved, even as the hopes for a resolution to the Cyprus issue would rise only to be dashed just as regularly during the Bank's five-year engagement.

The EBRD Annual Meeting in Warsaw sealed the agreement on EBRD engagement in Cyprus, securing the strong backing of the Governors.[20]

---

19 Jean Christou, 'Joint Declaration: final version as agreed between the two leaders', *Cyprus Mail*, 11 February 2014, https://cyprus-mail.com/2014/02/11/joint-declaration-final-version-as-agreed-between-the-two-leaders/.

20 EBRD Press release, 15 May 2014. 'EBRD shareholders agree to temporary financing for Cyprus'.

Bank of Cyprus rescue

Even before the vote on Cyprus had been taken, Georgiades made a comment that was to reflect strongly the actual outcome of the EBRD's activities on the island. "While EBRD operations in Cyprus are expected to be on a small scale and temporary, they would be of great significance."[21]

The EBRD's primary—and indeed very significant—contribution to Cyprus would in fact be rolled out very rapidly, even before the Bank had properly opened up its operations hub in Nicosia. On 29 July 2014, the EBRD announced it was investing €120 million in a €1 billion capital increase at Bank of Cyprus (BOCY).[22]

Bank of Cyprus was the country's largest financial institution, responsible for about 40 per cent of all banking assets, and only a year earlier it had been saved from collapse in an international rescue package and merged with the country's second largest bank which had been liquidated in the process. Recapitalisation of the banking sector was part of the agreement between Cyprus and the Troika.

Announcing the deal, the EBRD's First Vice President Phil Bennett said:

> This is our first investment in Cyprus and we are pleased that it allows us to apply our financial sector experience for the benefit of the country. Supporting the restructuring and recovery of Bank of Cyprus is critical for the economy as a whole. As an active shareholder, one of our priorities will be to work towards improvements in corporate governance. This successful capital raise is a positive signal to the markets, providing investors with additional confidence.[23]

Bank of Cyprus chief executive John Hourican called the capital raise a "turn the page" moment, while an editorial in the English-language business news site *Financial Mirror* referred to "a new era" for the bank.

Ironically, given the question over whether a country like Cyprus should be supported by the EBRD with its history dating back to the era of post-communist eastern Europe, the *Financial Mirror*'s piece had begun:

21 Speech to 2014 EBRD Annual Meeting.
22 EBRD Press release, 29 July 2014. 'EBRD participates in capital raise of Bank of Cyprus'.
23 EBRD Press release, 29 July 2014. 'EBRD participates in capital raise of Bank of Cyprus'.

> The rate at which Bank of Cyprus is witnessing successive 'new eras', one would think that we are a former Soviet state that has just come out of a rigid economic model and is suddenly embracing the free market system, with suitors lined up to buy anything they can get their hands on.

But, it continued,

> Now, nearly three years after the bank's foundations started to shake, BOCY seems to have at last completed its cycle and is about to embark on a truly new era, which, we hope will be an upward path and all stakeholders will get to benefit.[24]

The EBRD office in Nicosia was opened in December that year, in a ribbon-cutting ceremony attended by both Chakrabarti and Georgiades. Libor Krkoška, a senior banker at the EBRD, was in charge of the EBRD effort that set about building up the Bank's investment opportunities across the island.

A year after the investment in BOCY, which had been closely followed by EBRD support for a €1 billion mortgage covered bond issue, the Bank announced it was taking a stake in what was then the second largest commercial bank in Cyprus, Hellenic Bank.[25] The EBRD would also develop active support for trade finance and for small- and medium-sized businesses, rolling out an Advice for Small Business (ASB) programme in November 2015.

Unification hopes once again

The build-up to the EBRD's Annual Meeting in Cyprus in May 2017 coincided with another heady period of expectations about the possibility of a resolution to the decades-old dispute over the division of the island. Planned new talks were seen as the best hope of an agreement for many years.

The Annual Meeting underscored the Bank's commitment to continuing support across both the Greek Cypriot and Turkish Cypriot populated

---

24 'Cyprus Editorial: Yet another "new era" dawns for Bank of Cyprus', *Financial Mirror*, 30 July 2014, https://www.financialmirror.com/2014/07/30/cyprus-editorial-yet-another-aeoenew-eraae%C2%9D-dawns-for-bank-of-cyprus/.

25 EBRD Press release, 30 September 2015. 'EBRD becomes shareholder in Hellenic Bank'.

parts of Cyprus, with events—for the first time for any IFI—held in both south and north Nicosia, despite the protocol complications of providing access for staff and delegates across the Green Line.

The EBRD publicly threw its weight behind the unification process. In his opening address to the meeting, Chakrabarti emphasised his desire to see progress in reuniting the country:

> Our backing for economic integration across all our regions of operations is matched by our support for integration within the island of Cyprus itself. We have worked hard to fulfil the mandate set by our Governors to deliver projects across the whole island, for the benefit of both Greek Cypriot and Turkish Cypriot communities. The EBRD remains staunchly committed to promoting efforts towards unification.[26]

The President said he believed shareholders would be "strongly supportive" of extending the EBRD's mandate in Cyprus if negotiations on reunification succeeded and he held out the prospect of greater investment to address the transition challenges in the prospective united Cyprus should this come to pass.

One memorable feature of the conference was an exhibition game of basketball by the Peace Players Cyprus, a group of Greek-Cypriot and Turkish-Cypriot boys and girls united by the sport in their drive to play together, break down barriers and build relationships across the divide.

Just two months after the Annual Meeting, however, the latest hopes for lasting peace were again dashed when talks in the Swiss resort of Crans-Montana collapsed in failure.

Achievements in Cyprus

By the time the EBRD closed its office in Nicosia at the end of 2020, it had delivered just eight projects, worth a total of just under €600 million.

Sabina Dziurman, who was EBRD director for Greece and Cyprus, was adamant that even though the number of projects in Cyprus was low, the

26 EBRD Press release, 10 May 2017. 'Our work "will secure the EBRD's status as a strong and successful bank"'.

EBRD had left a lasting legacy on the island with its contribution to the Bank of Cyprus rescue.[27]

For Dziurman, the investment in BOCY was effectively an investment in the whole Cypriot economy: BOCY and the Cypriot economy were completely interlinked. "The fact that BOCY was rescued—and we played our part in that especially on the question of corporate governance—was a huge signal of confidence that helped the economy recover."

The government concurred with this view and highly appreciated the EBRD's contribution, according to Dziurman. "That came back from the Finance Minister," she said. "He told us: 'You were here when we needed you'."

There were other important contributions that transcend the bare figures.

With the island's history as a trading post, Cyprus had benefitted hugely from the EBRD's Trade Facilitation Programme (TFP) that promotes foreign trade to, from and within the EBRD's regions. The programme was rolled out very quickly in Cyprus and banks on the island became among its most active participants, helping the island's reintegration into global trade flows. Some €350 million of trade support was channelled to local banks in more than 650 transactions.

The EBRD also provided crucial support for Cyprus's small businesses, including many dynamic firms that needed better access to long-term funding and working capital or help to improve their marketing or efforts to innovate. The EBRD's Advice for Small Business programme, backed by donor funding, supported more than 270 small- and medium-sized enterprises across the whole of the island.

There was an important contribution to the decarbonisation of the Cypriot economy, too, with support for the development of renewable energy sources. One €10 million loan for the construction and operation of five solar parks in Cyprus made significant savings in CO_2 emissions and increased photovoltaic capacity on the island by 12 per cent.

One of the problems of doing more business in Cyprus was just how difficult it was to operate in the northern part of Cyprus. Unification of the island would have opened up many more opportunities to promote a market economy in a region that was far less advanced than the south.

A breakthrough on unification would almost certainly have meant the EBRD would have extended its term in Cyprus beyond the initial five-year

27 Interview, December 2020.

agreement, leading to increased investment in the northern part of the island. The case would have been very strong, since at issue was the prospect of de facto a new state, with the funding needs and transition gaps very different than those at the time of EBRD's initial mandate on the island.

There was no need for a 'graduation' debate or ceremony on departure as the arrangement had always been a temporary one. But the experience showed that the EBRD was adept at tackling specific problems where it could deploy its expertise, advice and capital in a targeted way to get a job done, even in an advanced European economy.

8. Towards Operations in Greece

There was no public discussion about the possibility of EBRD investment in Greece after the December 2013 talks in Athens. But the groundwork had been laid for taking the next step.

At the same time, the idea of possible direct involvement by the EBRD in Greece was becoming part of the overall response to the crisis from the European Union. A meeting of the Eurogroup in May 2014 indirectly touched on the idea—a proposal that the Greek authorities developed over the following months.

In its *tour de table* of various eurozone economies the Eurogroup gave a fairly upbeat assessment of the progress Greece had been making, referring to "recent positive macroeconomic developments in the Greek economy". A Eurogroup statement acknowledged the painful medicine the Greeks had been taking to deal with their huge economic challenge. "The renewed growth prospects for Greece reflect the remarkable adjustment efforts undertaken by the Greek citizens and authorities," it said.

The Eurogroup believed the Greek economy now had to take a new direction, with a new phase, moving from stabilisation and recovery to sustainable growth. Significantly, the finance ministers spoke openly about closer cooperation with IFIs. They did not refer specifically to the EBRD in their statement, but it opened a door to the possibility of its involvement:

> We recommend Greece, in coordination with the Commission (including the Task Force for Greece) to provide an overview of external financing

and technical support available and to reflect on the potential role of relevant international financial institutions in providing their expertise and, where applicable, funds.[28]

Shortly afterwards, the Greek authorities mandated the Board Director for Greece to prepare a study, coordinated with the European Commission's Task Force for Greece, of potential project-financing contributions that could be provided by the IFIs in support of the country's reform and growth agenda.

Nikolaos Dendias, the successor to Hatzidakis as Development Minister, drew on the Eurogroup statement in a letter to Chakrabarti in August 2014. There, Dendias made clear that Greece's structural reform agenda was incomplete and there were serious obstacles to recovery in economic areas where the EBRD could provide "valuable expertise and catalytic financial support".

Greece had indeed benefitted from the enhanced cooperation with the Bank, with support for Greek banking subsidiaries, co-investment with Greek corporates and the EBRD's promotion of cross-border infrastructure investments that involved Greece.

But now it was time for more. He asked the Bank to come up with an assessment of the different options for possible engagement, saying: "We would like to explore the possibility of EBRD investing directly in Greece, for a limited period of time, in order to support our programme of structural adjusted market-oriented reforms."[29]

In a statement to his fellow Directors, the representative for Greece, Anthony Bartzokas, gave a more detailed explanation of the Greek position. He noted that the enhanced relationship had been positive, but only up to a certain extent. "Looking back to what has been achieved in response to this initiative it is fair to say that the outcome of the continuous engagement with Greek banks contributed to the overall stability of the banking sector in the region."

But, he added, due to legal reasons it had been difficult for the EBRD to progress other areas, for example in trade finance, energy and transportation

---

28 Eurogroup statement on Greece: https://www.consilium.europa.eu/media/23910/eurogroup-statement-greece-2014-05-05.pdf.

29 Letter to the EBRD President from the Governor for Greece, 11 August 2014.

infrastructure. The EIB had provided a trade finance support line in response to an assessment of market gaps provided by the EBRD, for example.

Bartzokas stressed "at that point in time" the option of direct EBRD financing had not been considered, because the general understanding was that the main challenge for the Greek economy was macroeconomic adjustment—primarily tackling its twin budget and trade deficits. This of course was an issue "beyond EBRD's mandate and resources".

That had however changed with the suggestion that Greece review the potential role of the IFIs, including direct financing. There was a growing realisation that the rollout of structural reforms had to go hand-in-hand with investment financing. This was still weak in Greece because of the limited access of its banks and corporates to the capital markets.

The letter from the Greek Governor was part of this review process, Bartzokas said, and a welcome opportunity for an in-depth assessment of market conditions in the Greek economy.

Some controversy

Once again, as had been the case when the EBRD started discussions on engagement in Turkey, the debate about Greece initially led to divisions within the London-based EBRD Board of Directors.

Eurozone members had thrown their weight behind EBRD involvement, but some central Europeans in the EU were concerned that another potential expansion, this time into Greece, could mean less available financing for them.

It was clear, given the size of the Greek economy, that the EBRD would have to make a sizeable engagement. For it to operate effectively in the Greek economy, investments would—as indeed became the case—propel Greece to one of the top five EBRD recipients.

Some non-Europeans were initially sceptical. The idea of a long-standing EU country such as Greece becoming a country of operations raised many issues and could signal an end to the idea of graduation for obvious candidates among central European EU countries. Their opposition also reflected Greece's full integration within the EU and the eurozone.

Non-European critics saw the growing involvement of the EBRD in European affairs—especially in the context of an appeal from the Eurogroup of finance ministers—as an example of the Bank becoming an

instrument of EU policy. That threatened to undermine the EBRD's broad international nature with a mandate driven by shareholders from countries that spanned five continents.

Although reservations continued to persist, further missions were sent to Greece, with another report sent back to the Board in early November.

Bartzokas, reflecting in 2020 on those earlier developments, said the consensus that ultimately developed around a decision for the EBRD to invest in Greece reflected efforts to depoliticise the debate—to draw the discussion away from issues such as graduation and to focus wholly on the specific needs of the Greek economy and simply whether or not the EBRD could make a difference.[30]

The criticism and vocal caution continued but was primarily part of a process to ensure that strict limitations were put on what the EBRD would be allowed to do. As Bartzokas noted: "There was a consensus. But some shareholders continued to play a tough game in order to calibrate the scope of the activities as much as possible."

9. The Bank's Assessment

With that, the EBRD embarked on its assessment of how it could respond to the Greek request and the Greek authorities prepared to take whatever steps were necessary to reach a political consensus with the rest of the EBRD's shareholders.

In the report to the Board on 6 November 2014, management presented what it called a "compelling transition case to rebalance the (Greek) economy". The transition challenges facing Greece were comparable to those in many existing countries of operations, the report said. Privatisation had advanced only hesitantly and much of the economy remained in state hands. Equity markets were limited with private investors deterred by weak standards of corporate governance. The general business climate also remained problematic in several key areas, notably in contract enforcement.

Access to finance was an acute problem, especially for SMEs, the report continued. Critical infrastructure and important sectors like energy were dominated by the state, with limited room for commercialisation and

30 Interview, January 2021.

private sector involvement. This was a major obstacle to Greece's ambition of becoming a regional hub.

It was suggested that the EBRD's involvement could include steps to unlock the private sector's access to finance, including trade finance, and there would be direct support to medium to larger-sized companies and use of equity funds. It would also support the Government's privatisation programme, particularly in infrastructure and energy, and promote private sector participation. Energy efficiency was another priority identified. The Bank could also support capital markets through involvement in the issuance of corporate bonds.

The EBRD believed its temporary engagement would assist the turnaround in the economy. The proposed 5½ year investment period up until the end of 2020 was "short but manageable".

The Bank envisaged a potential annual investment volume of €500 million or perhaps slightly more, resulting in total investments during the whole period of engagement of some €3 billion, though amounts would depend on the pace of reforms and might be revised down if the reform environment was "unsupportive".[31]

10. Greece Formally Requests Country of Operations Status

The findings from the mission were also discussed in person the very next day with by now a third Development Minister and new Governor for Greece, Kostas Skrekas, at a meeting in the EBRD's London headquarters.

Skrekas wasted no time once back in Athens in formulating the official request to the Bank for Greece to become a country of operations. In his letter to the President, he put no specific time limit on the proposed temporary engagement, but referred to EBRD activities lasting for "only as long as is strictly necessary to help Greece address its transition challenges".[32]

Greece had clearly taken no chances about meeting resistance from other shareholders. The government's soundings and the minister's own discussions with Board members during his visit to London made Skrekas confident that there was broad support for the EBRD taking this next step.

31 Greece – Technical Mission, Board Information Session, 6 November 2014.
32 Letter from the Governor for Greece to the EBRD President, 25 November 2014.

With much of the spadework already completed with the production of the assessment paper on potential involvement in Greece, a resolution was very quickly drafted and presented to the Board of Directors. They would then vote on whether to pass the proposal to Governors for their approval.

The resolution should have gone formally to Directors on 14 January 2015, but there was a postponement after the US authorities requested more time for consideration, prompting an anxious letter from Skrekas stressing the acute need to support private investment and underpin resumption of growth in his country.

The original Board date for a decision was just 11 days before a 25 January election in Greece. One of the reasons for the call for a postponement had been political uncertainty ahead of the election.

As it turned out, the election result would change radically the face of Greek politics, end four decades of two-party rule and pitch a leftist administration into direct conflict with more economically conservative governments and authorities across Europe.

The Board remained focused on the issue at hand: making the EBRD's help available for fundamental structural reforms to the Greek economy. Once the outcome of the election was clear, and the uncertainties surrounding it over, the Directors approved the motion at the next available Board meeting, on 28 January.

The new administration very quickly re-confirmed the commitment to getting the EBRD on board in a letter dated 2 February. Three weeks later, on 27 February 2015, the Governors' resolution on Greece becoming a country of operations was passed.

Announcing the news, the EBRD President said:

> We are very happy to be able to apply our particular expertise in the private sector to the Greek economy. The EBRD will be fully engaged to make the most of its temporary mandate in the country. By concentrating on the private sector we are seeking to actively contribute to the reform and recovery of the country's economy.[33]

33 EBRD Press release, 3 March 2015. 'EBRD to invest in Greece'.

A period of volatility

The Greek election provided the clarity needed to allow the EBRD to move forward, but it was a prelude to a period of extreme economic volatility that persisted for much of the rest of the year.

The election victors were the left-wing Syriza party led by Alexis Tsipras who would immediately throw down an anti-austerity gauntlet to Greece's creditors in Europe. "Greece is turning a page," Tsipras said on the night of the vote, "It's leaving behind five years of humiliation and misery. … We are putting together a government of social deliverance to carry out our programme and negotiate with Europe."

The message to Brussels and Frankfurt, the seat of the ECB, was unequivocal: "The verdict of the Greek people ends, beyond any doubt, the vicious circle of austerity in our country."[34]

It was the start of frantic months in Greece, as the new government, including firebrand Finance Minister Yanis Varoufakis, bargained and battled with the EU, financial institutions and fellow European governments.

They marched many times to the brink of a precipice only to march back again. The brinkmanship included putting the terms of a bailout package to the people, winning a referendum on 5 July with a resounding "no" to austerity, only to return to the table to accept the terms of a new bailout that very same month.

The summer was spent pushing the new rescue package through parliament after which a new election was called that returned Tsipras to office, but with a shrunken majority. Varoufakis, who had resigned straight after the referendum, compared the new bailout terms to the Versailles Treaty that had humiliated and punished Germany after World War I. Feelings were certainly running high, but objectively Greece needed investment more than ever.

11. EBRD Steps In to Bolster Greek Banks

The EBRD was now free to start looking for investment opportunities. But the mood of the Board was unsurprisingly one of caution. Even under

---

34 Tony Barber and Kerin Hope, 'Syriza win throws down challenge to Europe', *Financial Times*, 26 January 2015, https://www.ft.com/content/9610da8a-a496-11e4-8959-00144feab7de.

normal circumstances, proposals for relatively uncontroversial transactions such as trade facilitation were subject to intense shareholder scrutiny.

As with Cyprus, the first big EBRD investment in Greece targeted the troubled banking sector. Dziurman had taken up her position as Director for Greece and Cyprus, based in Athens, in early September 2015.

Just two months later, the EBRD announced a €250 million financing package for the country's four systemic banks, which involved the Bank buying stakes. It was one of the most controversial set of transactions that the Bank had ever undertaken.

A review by the ECB had identified a potential capital shortfall of €14.4 billion for the four banks.

The EBRD's funding supported a multi-billion euro recapitalisation of Alpha Bank, Eurobank, National Bank of Greece and Piraeus Bank and gave the EBRD the opportunity, as a shareholder, to play an active role, especially in corporate governance.[35]

At the time, Nick Tesseyman, the EBRD's Head of Financial Institutions, described the recapitalisation of the Greek banks as an essential step towards the recovery of the country's economy: "With our involvement we are demonstrating our commitment to contributing to this process and we will play an active role as a shareholder so that the four banks can provide the real economy with finance again."

Dziurman recalls that between the go-ahead for the EBRD to invest in Greece and the start of those operations much had changed, not least as a result of the election of the new government and the further explosion of the country's debt crisis.

Events in the country moved very fast between her appointment earlier in 2015 and actually taking up her position in September. There were occasional doubts as to whether the new party in power actually wanted the EBRD's participation. Would the EBRD be investing in a country with the euro as its currency, or would it be the drachma again if Greece exited the eurozone?

Dziurman said that she and her team were starting work on the basis of an investment plan that did not reflect the changing circumstances in Greece. She was in the country, building up a team, with a pipeline that was now out of date. The country assessment for Greece presented to the shareholders before they decided to agree to EBRD investment had not focused

35 EBRD Press release, 25 November 2015. 'EBRD to become stakeholder in Greece's four systemic banks'.

particularly on the financial sector, precisely the area where the EBRD had now made its first very significant investment.

The assessment had put an emphasis on the Bank helping to unlock the private sector's access to finance and supporting private sector participation and commercialisation of infrastructure to enable regional integration and improving the quality of utility services.

"There was a lot of rejigging," Dziurman said. There had originally indeed not been a focus on banks. "But that had changed," she said.

By the time the first country strategy was published in June 2016, the picture looked different. Supporting the stabilisation of the financial sector was one of the strategy's key priorities, as well as supporting private Greek companies and helping them realise their export potential. Promoting private sector participation in and commercialisation of the energy and infrastructure sectors remained a target and subsequent efforts to encourage regional integration yielded some positive results.[36]

In the context of private sector involvement in the energy sector, Dziurman highlights the EBRD's role in the privatisation of the country's gas grid operator DESFA as a major success. The EBRD took part in the bidding for a stake in DESFA in 2018. It was not part of the winning consortium, but the fact that it participated at all contributed to the success of the sale, in terms of delivering a good price for the state. "Our presence turned this into a truly competitive tender."

12. An Extended Mandate

By 2018, the EBRD had become a very important player on the Greek market. Total investments for that year would amount to €846 million, making it the third largest recipient of annual financing after Egypt and Turkey, but the Greek government felt that the Bank could contribute beyond its 2020 remit.

A letter requesting an extension of the mandate came on 13 March 2018 from Development Minister Yannis Dragasakis. He said Greece and the EBRD could be proud of their joint achievement over the previous three years. Further,

36 EBRD Press release, 23 June 2016. 'EBRD adopts strategy for Greece'.

> In our view—and this view is very much shared across the political spectrum in Greece—there is still much more that the EBRD could do to help Greece address its transition challenges and assist it in the private sector investment. There is also scope for working with us, alongside other key partners, on new plans, as we develop them, to intensify the integration of Greece within the wider region of South Eastern Europe.[37]

The original resolution allowing Greece to become a country of operations had stipulated that any request for an extension had to be presented to the 2020 Annual Meeting. But the Greeks wanted to move faster than this. "It would be good if the Governors could make a decision already at the Annual Meeting in Jordan later this year," Dragasakis wrote. That would have meant taking a decision in just two months in time for the meeting in May.

Chakrabarti flew to Greece in March for talks with Tsipras and other key ministers to discuss the question of an extension of the mandate. Reflecting on the progress to date, he said during the trip:

> In less than two and a half years we have invested €1.6 billion in the Greek economy and Greece has become [on basis of 2017 financing figures] the fifth largest country in which we invest. This demonstrates what the EBRD can do and illustrates our commitment to the country, one of the founding members of our institution. If our shareholders agree, we are ready to work with the Greek authorities to extend our mandate to support economic recovery.[38]

There was a lot of back of forth between management and Board Directors about the timing of a decision on any extension. Some Directors were pointing firmly to the original insistence that an extension could not be requested before the 2020 Annual Meeting.

There was a decision at the EBRD Annual Meeting in Jordan in May 2018, but only for the Governors to ask the Directors to review the request and come back before the end of the year to seek further guidance on whether or not to extend Greece's recipient status.

---

37 Letter from the Governor for Greece to the EBRD President, 13 March 2018.

38 EBRD Press release, 27 March 2018. 'EBRD President Chakrabarti in talks with Greek authorities'.

In its report in September to inform that review, management noted that the Bank had begun its operations in Greece in the first half of 2015 at a time of considerable turbulence in the country, culminating in the temporary closure of the banking system and the introduction of capital controls. While relative calm was restored by the second half of 2018, growth remained elusive for some time afterwards and investment and confidence levels remained subdued as Greece struggled to emerge from the crisis.

Greece had only exited its latest rescue programme a month earlier, in August 2018, and still faced important challenges. The country continued to need substantial investment that was only likely to come from external sources and reforms that had been initiated during the adjustment programme still had to be implemented. Encouragingly, as part of its new growth strategy, Greece intended to promote regional cooperation and intensify efforts to develop interconnections with neighbouring countries in south-eastern Europe. As Chakrabarti made clear in his recommendation to the Board: "Addressing these challenges is key to making Greece more resilient. It will take several years to do so effectively, and the Bank is well placed to continue to assist Greece in the three targeted areas."

Looking back, Dziurman said the extension was clearly justified by the events in Greece as the EBRD had started its work there, and as the Bank adjusted to the changing needs of the economy and the new government settled in. "There had been delays. We had lost a bit of time out of the five years. We'd obviously managed to find opportunities and we had built the foundations that meant we could do more."

By early December 2018, with the Governors on board, the EBRD could announce the extension. Commenting on the successful endorsement of the Bank's further engagement in Greece until 2025, the President said:

> With its investments and support for Greece so far, the EBRD has demonstrated its ability to respond quickly to the country's economic requirements. The extension of the mandate illustrates our continued commitment. We are now ready to do more to support Greece in its economic recovery.[39]

Announcing the extension, the Bank referred specifically to its achievements in the stabilisation of the banking sector, its participation in the

39 EBRD Press release, 4 December 2018. 'EBRD extends its mandate in Greece'.

modernisation of regional airports, a framework for renewables, the launch of a programme of support and advice for small- and medium-sized enterprises and its support for Greek banks to resolve the challenge of high levels of non-performing loans.

Dziurman adds that the EBRD engagement was very market oriented. "What we ended up doing a lot of in Greece were market transactions. We did a lot of bonds."

With its investments in corporate bonds listed on the Athens Stock Exchange, the EBRD made an important contribution to the development of the local capital market. It also supported the access of Greek firms to the international capital markets with its participation in a number of Eurobond issues. By 2020, the EBRD had invested well over €600 million in around 20 domestic and international bond deals, worth a total of more than €9.2 billion.

In an interview with the Greek newspaper *Kathimerini* on 27 January 2019, Bartzokas underlined the reasons for a continuing Bank presence:

> The EBRD's successful involvement in Greece confirms the scale of investment needs and the feasibility of launching financing structures with sound market economics criteria that mobilize private capital and enhance the prospects for economic growth.[40]

When asked in 2020 to provide an overall assessment of EBRD's engagement in Greece, Bartzokas told the same newspaper:

> The successful operation of the EBRD in Greece is a testament of the need and the feasibility of market-based solutions for investment recovery. If we consider that the EBRD's investments are private sector oriented, with an estimated threefold capital leverage, we can conclude that untapped opportunities are at the disposal of policy makers for investment recovery in the Greek economy.[41]

---

40 Evgenia Tzortzi, 'EBRD's long-term investment in Greece', *eKathimerini*, 27 January 2019, http://www.ekathimerini.com/237076/article/ekathimerini/business/ebrds-long-term-investment-in-greece.

41 Evgenia Tzortzi, 'Economic crisis experience key in battling Covid fallout, says EBRD official', *Ekathimerini*, 11 June 2020, https://www.ekathimerini.com/253538/article/ekathimerini/business/economic-crisis-experience-key-in-battling-covid-fallout-says-ebrd-official.

By the end of 2020, the EBRD had invested a total of over €4 billion in Greece and had a substantial portfolio of €2 billion, overwhelmingly in the private sector.

The rapid build-up in business showed that the EBRD had repaid its shareholders' faith in its abilities to deliver change on the ground through its investments and expert sectoral and policy advice.

Shareholders had taken on serious risks in pressing the "go" button at a time of great turmoil and economic uncertainty, but the rewards were there for all to see with good prospects of more successes to come in the future.

Chapter 5

Geopolitical Tensions

Introduction

Two decades after the fall of the Berlin Wall, the EBRD had begun to invest in a new range of countries located on the borders of the European Union and across the Mediterranean Sea. The addition of these countries—Turkey, Egypt, Jordan, Tunisia, Morocco, Cyprus and Greece—increased the population in the Bank's ambit by more than two-thirds. The Bank's operational compass had swung significantly towards the south. But it was events related to Russia that made this shift decisive.

Russia's share of annual Bank business had already begun to wane by 2007, from a level of just over 40 per cent. After the annexation of Crimea in 2014 and the imposition of EU sanctions on Russia, shareholder guidance interrupted the flow of investments. From that July, new EBRD business in Russia dropped away to zero; and the portfolio shrank from an earlier peak of around €10 billion to little more than €1 billion by the end of the decade.

A series of events linked to Russia contributed to this situation, starting with a conflict in Georgia, followed by the seizure of Crimea and escalating with military engagement involving Russian-backed rebels in eastern Ukraine. It would lead to disputes with Russia at the Board for a number of years and a difficult period for the EBRD's President and its management.

Although the Bank would survive unscathed in overall business volume terms, which continued to grow steadily, the absence of new activity in Russia represented a radical departure from the EBRD's previous strong engagement with the Federation. Investment and reform at centre of the former Soviet Union had after all been a key driver of the Bank's transition mission; and Russia was its biggest client by far.

Resources allocated to help Russia's development now shifted towards the Mediterranean region. The transition needs of the new countries, especially given their rapidly growing populations, were large. It therefore made eminent sense to redeploy the EBRD's efforts and ramp up business in this region while also continuing to pay attention to countries where transition progress had been slow, such as in Central Asia.

The demise of Russian operations was undoubtedly a disappointing coda to a relationship that over the years had benefitted both sides well. But circumstances had changed and the growing gap became increasingly unbridgeable.

Russia nonetheless continued to play a significant role as a strong and vocal member of the Bank giving all EBRD members through its Board Director the benefit of its knowledge, especially on transition challenges facing newer countries of operations.

Events in this story begin in the dog days of summer 2008 in Tskhinvali, the capital of South Ossetia, a separatist area of Georgia close to the border with Russia.

1. The Crisis in Georgia, 2008

Around the middle of 2008, the Georgian economy was performing strongly. Under flamboyant President Mikheil Saakashvili, the country had introduced a series of reforms aimed at improving the business climate and attracting more investment. The banking sector had strengthened significantly over the previous two years and a new regulatory agency was beefing up supervision across the financial sector.

Saakashvili was presiding over what was viewed as an unparalleled success story in the region, a paragon of private sector-led transition. Foreign direct investment in Georgia had risen dramatically, reaching almost 20 per cent of GDP in 2007, or nearly US$ 2 billion, and remained vigorous into 2008. In April, Georgia issued its first sovereign Eurobond, raising US$ 500 million, which was heavily oversubscribed. Since Saakashvili took over as President four years earlier, the economy had expanded at an annual rate of over 10 per cent and was running at a robust 8.5 per cent rate in the first half of the year.

This rosy economic scenario, however, belied a more sinister geopolitical backdrop of growing tension between Georgia and Russia over two

breakaway republics in Georgia and Georgia's desire for membership of NATO. Relationships had long been strained and the tension erupted into war between the two countries on 7 August 2008. There was an immediate impact on the economy, with GDP falling by over 6 per cent in the third quarter, and especially on Georgia's banking system.

Even before G7 Finance Ministers on 20 August called for a strong response by IFIs –including by the EBRD[1]—the Bank was on the ground talking to clients, preparing financing packages and coordinating its response with the international community. The EBRD saw its role as particularly important in order to preserve as far as possible Georgia's private sector-led growth model.

EBRD staffers look back at the occasion as an important moment when the Bank came into its own in defence of the economy and financial system of one of its countries of operations at a time of crisis.

Although small in comparison with other countries of operations, Georgia was significant because it had been very successfully following a reform path, one which the EBRD had been supporting. Bank activities in the country had increased rapidly during this time with the portfolio more than quadrupling between 2004 and 2008 to almost €400 million. The conflict and its consequences threatened these achievements.

For a poor country in the Caucasus, the effects of the war were serious with tens of thousands of its citizens displaced or made homeless. The immediate humanitarian task was for others to deal with. But the Bank could see that failure to stabilise the economy would bring further disaster and there was a need to help reconstruct damaged infrastructure and housing. As an important energy transit region, Georgia's future depended on a swift restoration of business.

Bank teams were quickly mobilised. UK-based staff were brought back from their summer holidays for meetings at EBRD headquarters to map out a response, with a suitable action plan and communications strategy. The resident office in Tbilisi was on high alert and ready to respond. Some staff evacuated their families. Nonetheless, Bank business carried on, with the office only shutting its doors for one day.

---

1 "We ... call on the Georgian authorities, other countries, the World Bank, European Bank for Reconstruction and Development, Asian Development Bank, European Investment Bank, and European Commission to promptly identify and support reconstruction needs and the restoration of services that will build a base for future economic growth." G7 Finance Ministers' statement, Washington DC, 20 August 2008, Munk School, University of Toronto.

Local and international staff worked round the clock to deal with the immediate challenges—both in the jeopardised banking sector and across the country's damaged infrastructure. A crisis-response template was created which had lasting benefits—it turned out the global financial crisis was only weeks away.

2. Georgia and NATO

Saakashvili had swept to power aged just 36 in 2004, after the 'Rose Revolution' that ousted Eduard Shevardnadze, the former Soviet Foreign Minister whose presidential administration of Georgia was tarnished by allegations of corruption and vote-rigging. After winning the presidential election on 4 January, the reform-minded US-educated lawyer pledged to push for closer ties with the USA and Europe and to stamp out the corruption that had hampered economic progress. He had been determined to radically modernise the Georgian economy and to make it a magnet for external investment.

Lado Gurgenidze, who became Prime Minister of Georgia in late 2007 after heading Bank of Georgia, the largest bank in the country, has no doubts about the success of the policies that were introduced in the wake of the revolution. "The economy was doing phenomenally well," he said. There had been massive deregulation, aggressive privatisation and a radical simplification of the fiscal regime that produced low and flat taxes. At the same time, the government had been in a position to deliver funding for social assistance, welfare and healthcare on the back of a six-fold rise in tax revenues.

On the external front, since taking power Saakashvili had pursued a dual strategy that sought to reduce the tensions with Russia while he simultaneously wooed the NATO alliance.

Nonetheless, tensions with Russia increased during the four years of Saakashvili's first term as he guided Georgia towards NATO and because of Russia's support for the breakaway regions of South Ossetia and Abkhazia, where Moscow stationed peacekeeping troops.

The war of words intensified, partly as Russia linked a bid for independence from Serbia by Kosovo to developments in the two rebel regions in Georgia. Russia was fiercely opposed to independence for Kosovo, making clear that if Pristina could take this step then South Ossetia and Abkhazia could secede from Georgia.

Kosovo formally declared independence on 17 February 2008 (and is still not recognised by Russia). At the same time, Tbilisi was actively pursuing NATO membership, a goal that Moscow firmly rejected both for Georgia and for fellow former Soviet republic Ukraine. These moves worsened relations with the West. A Reuters briefing summarised the picture: "The West's recognition of Kosovo's declaration of independence from Serbia in February 2008, over Russian objections, fueled tensions and in April NATO pledged future accession for Georgia and Ukraine, angering Moscow."[2]

By this stage, a number of former communist countries had signed up to NATO, including Poland, Hungary and the Czech Republic. In another round, in 2004, they were joined by Bulgaria, Romania, Slovenia, and the Slovak Republic—and also the Baltic States.[3] NATO membership was firmly on the agenda for Ukraine and Georgia, but Russia was adamantly opposed. NATO itself was split, with the US and former communist members in favour and some of the western Europeans nervous about antagonising Moscow.

At a NATO summit in April 2008 in Bucharest, the western alliance invited Croatia and Albania to join the alliance, which they did a year later. An invitation to what was then formally called the Former Yugoslav Republic of Macedonia would have to wait until a dispute about the name of the country with Greece was resolved.[4] Neither Georgia, nor Ukraine received the firm invitation accorded to Croatia and Albania. While NATO's language was strong and supportive, further assessment was put off until the end of the year.

Pressure from Russia continued, however. By the middle of April, Moscow was strengthening its ties to South Ossetia and Abkhazia in what Georgian Foreign Minister Davit Bakradze said amounted to a "legalisation of the de facto annexation process" by Russia. The NATO alliance said it was deeply concerned and called on Moscow to reverse the legal ties that had been established.

---

2 'Facts about the 2008 war in Georgia', *Reuters*, 4 August 2009. https://www.reuters.com/article/us-georgia-war-conflict-sb-idUSTRE5732TH20090804.

3 To this day, Latvia, Lithuania, and Estonia are the only former Soviet states to have become members.

4 North Macedonia became a member in 2020.

3. Conflict in South Ossetia and its Impact

As spring turned to summer, both sides turned up the rhetoric and the build-up of their forces, with fighting erupting between Georgian troops and separatist forces in early August 2008. Georgia launched a campaign against Tskhinvali, on the evening of 7 August. Russia responded by sending tanks into South Ossetia, ostensibly to support Ossetians who were Russian citizens on the basis of their Russian passports.

The Russian assault went beyond the confines of South Ossetia, with a push into Georgia to within just 25 miles of Tbilisi. After five days of fighting, a ceasefire agreement was negotiated on 12 August between Russian President Dmitry Medvedev, Saakashvili, and French President Nicolas Sarkozy, on behalf of the European Union. Following the ceasefire, Russia recognised the independence of South Ossetia and diplomatic ties between Tbilisi and Moscow were severed.

An official EU fact-finding report issued a year later blamed both parties for the conflict, which it said had left nearly 850 people dead and 35,000 Georgians homeless and in which thousands of Georgians had tried to flee to either Armenia or Azerbaijan.[5]

During the conflict, the EBRD called for a rapid resolution in a public statement that referred to the enormous progress Georgia had made with reforms that had helped the economy develop, attract investment and deliver an efficient, well capitalised and robust banking sector. The Bank reinforced its message, saying: "The EBRD will continue to stand by its partner banks in difficult times and to work on active prospective projects in the Georgian financial sector."[6]

The conflict with Russia had an abrupt and severe effect on the economy. The stock market fell sharply and international reserves dropped by one-quarter, tens of thousands of Georgians withdrew cash from their bank accounts threatening the banking system[7] while transport routes between Poti, Georgia's main Black Sea port, and Tbilisi were cut off, creating a

5 EU Council (2009), Report of the Independent International Fact-Finding Mission on the Conflict in Georgia: https://www.echr.coe.int/Documents/HUDOC_38263_08_Annexes_ENG.pdf; 'Quotes from EU-sponsored Georgia war report', *Reuters*, 30 September 2009, https://www.reuters.com/article/uk-georgia-russia-report-highlights/quotes-from-eu-sponsored-georgia-war-report-idUKTRE58T3SU20090930.

6 EBRD Press release, 11 August 2008. 'EBRD urges rapid resolution of Georgia conflict'.

7 Bank deposits fell by 14 per cent within two weeks according to National Bank of Georgia figures.

bottleneck for many products.[8] Georgia's vital tourism industry was also badly affected as was confidence in the economy more generally.[9]

Georgia's fast-growing economy, which had been pulling in very large amounts of FDI in the previous two years, was facing a difficult future. "That FDI disappeared overnight," Gurgenidze recalls.[10] Georgia was experiencing a domestic recession. "Banks were sitting on a bunch of non-performing loans," he adds. Gurgenidze pointed further to infrastructure damage worth around US$ 1 billion equivalent to nearly 10 per cent per cent of Georgia's GDP of just US$ 12 billion.

In the wake of the conflict, the EBRD quickly linked up with the IMF, with whom contacts in the region were particularly good, and engaged with the World Bank and UN in a Joint Needs Assessment (JNA) for Georgia that also involved the Asian Development Bank (ADB), the European Commission, the EIB and the IFC.

The scale of Georgia's needs was soon established. Budgetary shortfalls, infrastructure and social sector spending were estimated at some US$ 3.25 billion over three years, with additional funding of US$ 700 million needed to keep the banking sector afloat. The IMF provided an exceptional access Stand-By Agreement in September,[11] which helped cover external financing gaps and stem the decline in confidence, while in October international donors pledged support totaling US$ 4.5 billion.[12]

Catarina Bjorlin Hansen, in 2020 the regional EBRD Head for the Caucasus, had been an infrastructure banker based in Tbilisi back in 2008. She was out of the country when the conflict began but took the first flight back to Tbilisi. "There was definitely a fighting spirit," she recalls, as teams were galvanized into action. "We toured the whole country by car, looking across the cities of Georgia to see what had been damaged, destroyed and what

8 See 'Georgia: Request for Stand-By Agreement', IMF, 10 September 2008, https://www.imf.org/external/pubs/ft/scr/2008/cr08328.pdf; and Dan Bilefsky, 'War Left Georgia Economy Bruised, but Not Broken', *New York Times*, 27 September 2008, https://www.nytimes.com/2008/09/28/world/europe/28georgia.html.

9 Spreads on Georgia's sovereign bonds rose by 240 basis points at their peak, to 775 basis points above comparable US Treasuries. Georgia's sovereign and banks' external debt ratings were also downgraded. See 'Georgia: Request for Stand-By Agreement', IMF, p. 10.

10 Interview, 2021. Note that the authorities and IMF staff predicted a drop in private inflows—FDI, bank lending and portfolio investment—of over US$ 1 billion in the second half of 2008, of which about half was expected to result from lower FDI. See 'Georgia: Request for Stand-By Agreement', IMF, pp. 12–13.

11 An 18-month programme of 317 per cent of quota, worth around US$ 750 million and equivalent to 7.5 per cent of Georgia's 2007 GDP, was approved on 15 September 2008.

12 Approximately US$ 2 billion in grants and US$ 2.5 billion in loans.

needed to be rebuilt," she says. "On my birthday, I inspected a bombed-out waste water treatment facility."[13]

The tour was an opportunity to make an in-depth assessment of the whole infrastructure challenge across Georgia, looking to make improvements in both the conflict areas and the areas which still needed work following the neglect of the Soviet era. It was important to make sure post-conflict reconstruction in the war zone did not lead to regional imbalances. According to Bjorlin Hansen, this exercise laid the ground for many of the infrastructure improvements that are visible in Georgia today.

A major part of the EBRD's response to the crisis involved decisive support for the banking sector that is still remembered over a decade later by local financial sector leaders.

The JNA report, presented to donors in Brussels in October 2008, said the conflict had dealt a shock to the key pillars of economic growth across Georgia. There had been a weakening of investor, lender and consumer confidence, a contraction of liquidity in the banking system, stress on public finances, damage to physical infrastructure, and increased numbers of internally displaced persons.

The report said the banking sector had weathered the immediate impact of the conflict but referred to near-term post-conflict challenges. Key banks faced external obligations falling due in early 2009. The economy had experienced an increase in the demand for dollars and withdrawal of deposits from the banking system. The report also drew up an assessment of the sector's financing requirements, estimated at some US$ 700 million in short-term finance in order to allow a rollover of liabilities and to provide support for a moderate growth scenario. It said these could be satisfied by a combination of equity and debt finance as well as guarantees by international financial institutions and by donors.

4. The Bank's Response

The EBRD was preparing to address these needs well before the publication of the report. Just one week after the Russian invasion, Nick Tesseyman, newly appointed as Managing Director for Financial Institutions, was

13 Interview, 2020.

in Tbilisi with a team working with the EBRD's eight partner banks and developing a range of fast disbursing support facilities, in particular for the country's two leading banks, Bank of Georgia and TBC Bank. The purpose of these facilities was to provide essential liquidity and an important buffer against the effect of a sudden downturn in activity across the economy.

The very fact that the EBRD was in Georgia early on and actively working with the banks was a calming signal. By September the outline of financing for Bank of Georgia had been prepared and the whole process was approved by the Board in November. As one banker active on the deal later commented, "The EBRD's response was in time to shore up Bank of Georgia's balance sheet."

The EBRD together with the IFC provided a US$ 200 million financial package to Bank of Georgia that was made up of subordinated, convertible and senior loans that offered longer-term liquidity and allowed the bank to continue lending to retail clients and SMEs, key drivers of economic growth in Georgia. At the time it was the EBRD's largest transaction in the financial sector in the early transition countries (ETCs), which are among the poorest countries where the EBRD invests. The financing helped Bank of Georgia recover from the crisis and to promote a stable and healthy banking sector.

TBC Bank, the second largest in Georgia, with which the EBRD had begun a relationship based around trade finance back in the late 1990s, received US$ 70 million in a financing package that comprised two loans and an equity stake worth US$ 36.8 million.

Bank of Georgia and TBC Bank dominated the Georgian banking sector, representing up to 70 per cent of the banking market. For Gurgenidze it was quite clear that not one but both of these banks could have collapsed given the size of the economic shock from the war and the growing global crisis. He said: "Specifically, the EBRD—together with the IFC—in the immediate aftermath of the war were instrumental in helping to avert a banking crisis. They played a very important role."

This support sent an important signal at a time of investor anxiety caused by the war, especially given the downgrades imposed after the outbreak of hostilities by the rating agencies Fitch and Standard & Poor's.

On 5 September, EBRD management presented to its Board proposals for a response to the challenges to growth from the conflict and its negative impact on investor confidence. The Bank made clear it would continue

to support its partners and help the local economy regain its momentum, so Georgia could again become a stable and attractive location for foreign investments. In accordance with its three governing principles,[14] the EBRD outlined a three-pronged approach that entailed maintaining the higher level of investments already envisaged in the 2008 business plan, as well as offering co-financing in new infrastructure funds and actively participating in the IFI/donor needs assessment steering group with the specific aim of making sure responses did not crowd out the private sector.

Another positive that arose out of this difficult period was enhanced cooperation among the donor community and development organisations like the EBRD in Georgia. "This conflict paved the way for donor coordination in Georgia," said Bjorlin Hansen, "raising it to a completely different level and resulting in the excellent cooperation that we have in this country today."[15]

The EBRD's response to the conflict in Georgia was underway as the global financial crisis was escalating and just days before the collapse of Lehman Brothers on 15 September 2008 sent emerging economies into a tailspin. The experience was put to good use in this new context. The combination of IFI and donor efforts and the effective response of the Georgian authorities to their predicament was decisive in ensuring Georgia's situation stabilised and that the economy returned to a steady growth path further ahead, one that outperformed its peers in the longer term.

5. Ukraine and Russia, 2014

On 23 July 2014, the EBRD issued a short statement that would test relations for years to come with the very country that until then had been the largest single recipient of its investments. The Bank was being drawn into a geopolitical crisis that was reverberating around the globe.

It was a development that would also radically change the EBRD's investment portfolio, signalling and sealing a further dramatic shift in the

14 Transition impact, additionality, and sound banking. In the latter case the IMF US$ 750 million macroeconomic stabilisation package was seen as key by providing vital external finance and liquidity to the heavily-dollarised Georgian economy.

15 The JNA, to which the EBRD contributed, was named as one of the winners in the World Bank's third annual competition 'Improving the Lives of People in Europe and Central Asia' in 2010. See 'Georgia Post-Conflict Joint Needs Assessment Wins a World Bank Prize', World Bank Press Release, 31 March 2010.

geography of the Bank's activities away from the cradle of its inception, the former communist countries of eastern Europe

On that day, the EBRD effectively ceased new financing in Russia—not as a management decision but following guidance from a majority of its Board of Directors that they would "for the time being" be "unable to approve new investment projects in the Russian Federation".[16]

Annexation of Crimea and armed conflict in eastern Ukraine

The guidance followed an angry response by the EU and the USA to the escalating tensions between Russia and Ukraine. In March 2014, Russia had annexed Crimea, which had been part of Ukraine since the 1950s. Shortly afterwards Russian-backed separatist rebels and Ukrainian forces were waging an increasingly violent war in eastern Ukraine.

On 16 July, the EU called on both the EBRD and the EIB to halt financing to Russia when it announced a series sanctions aimed at Moscow.

Western anger against Russia rose dramatically just one day later when a Malaysian airliner en route to Kuala Lumpur from Amsterdam was shot down over Ukraine. All 283 passengers, the overwhelming majority of whom were Dutch citizens, and 15 crew were killed. A Dutch-led investigation team concluded that flight MH17 had been hit by a Russian-made Buk missile fired from a field in eastern Ukraine controlled by the rebels.

The halt to new EBRD financing was perhaps just one small piece in the complex mosaic of fraught relations between Russia and Ukraine and between Russia and the West. It was, however, a step that some at the Bank initially feared might prove existential.

The importance of Russia to EBRD business

Russia was a crucial integral part of the EBRD's operations. By far the largest economy within its region, Russia consistently received the highest annual share of EBRD investments and the Bank was the most important international investor in the country outside of the oil and gas sector.

---

16 EBRD Press statement, 23 July 2014. 'EBRD statement on operational approach in Russia'. Council on Foreign Relations (CFR): https://www.cfr.org/backgrounder/ukraine-conflict-crossroads-europe-and-russia.

By 2013, the EBRD had invested over €23 billion in Russia in more than 700 individual projects. Concerns had been expressed during the latter part of the first decade of the 21st century that the EBRD was becoming over-dependent on Russia. In absolute terms, the peak of EBRD investment had been in 2011, when Bank financing was some €2.9 billion out of a total of just over €9.0 billion. As a share of investment, however, Russia had taken over 40 per cent of total financing in 2007. The share had been steadily and deliberately reduced in subsequent years. One of the arguments for entering the Turkish market in 2009 had been to create a more balanced portfolio as a counterweight to the dominance of Russia.

In 2013, however, the Bank was still expressing a strong commitment to its continued presence in Russia. "We are proud of the role we play here and will continue to play in the further long-term development of the Russian economy," Chakrabarti told a meeting of the Russia-Singapore Business Forum in September of that year.

The EBRD strongly believed that its private sector-focused investments could support the growth of a burgeoning middle class in Russia that ultimately would build a counterweight to the pervading role of the state in the economy. It aimed to bolster the reformers, strengthening the role of private sector players that would keep demanding a level playing field, respect for property rights and the rule of law.

The EBRD strategy at the time made this clear:

> The Bank will pay particular attention to projects that increase economic opportunities for the emerging middle class in the regions through increasing access of regional SMEs to finance, supporting urban renewal, and improving the quality of jobs and services.[17]

Bank financing was overwhelmingly in the private sector. Of its investments in the six months up to the financing halt in July 2014, 88 per cent had been private sector projects.

There were undoubted challenges to investment in Russia, not least of which was corruption. Nevertheless, Chakrabarti made clear in his speech to the forum that the EBRD was going to stay in Russia and was there for the long haul.[18]

---

17 EBRD Country Strategy for Russia: https://www.ebrd.com/downloads/country/strategy/russia.pdf.

18 EBRD Press release, 23 September 2013. Speech transcript, 'EBRD is fully committed to Russia'.

The halt in financing to Russia in 2014 starkly underscored the shift in the EBRD's activities that had been signalled in 2008 when shareholders agreed that the Bank would invest in Turkey, meaning for the very first time the EBRD would venture beyond the confines of the former communist east.

At the end of 2013, before the financing halt the Bank's portfolio of investments in Russia stood at €8.9 billion, by far the largest individual holding. Just one year later, annual investment to Russia would fall to €608 million from €1.8 billion in 2013. In that same year, Turkey became the Bank's single largest country of operations by annual investment volume, with a total of just under €1.4 billion.

Six years later, with no new investments since July 2014 in Russia, and as loans were repaid and shareholdings wound back in the normal manner of business, that portfolio had shrunk to just under €1.2 billion, dwarfed by the relatively newer geographic investment destinations. Turkey now accounted for the lion's share, with a portfolio close to €7 billion. The holdings in Egypt had risen to close to €4.5 billion.

6. Deep and Persistent Corruption

The Yanukovych era

For all the later tensions with the Moscow authorities that would emerge from the halt to investments linked to events in Ukraine, a year earlier in 2013, it was in fact Ukraine that was causing the EBRD the most problems.

In 2010, Viktor Yanukovych had taken over the Presidency of Ukraine from Viktor Yushchenko. It was Yanukovych's second shot at leadership. An earlier election victory in 2004 against Yushchenko had been overturned amid allegations of fraud and voter intimidation that triggered the 'Orange Revolution' from which Yushchenko emerged as a hero.

During his period in office, Yushchenko pinned his colours firmly to the mast of closer integration with the West. He regularly stressed the importance of Ukraine joining both the EU and NATO, a position that Moscow continued to resist. He criticised Russia's incursion into Georgia in 2008 and annoyed Moscow by insisting that Russia remove its Black Sea fleet from Crimea by 2017.

When Yanukovych assumed power in 2010, primarily with the support of Russian speakers in the industrial east of Ukraine as well as in the south including in Crimea, he was determined to mend the relations with Moscow that had soured significantly under Yushchenko. Equally, he knew he had to play both sides of the geopolitical equation.

In a low-key inauguration ceremony that was boycotted by his 2010 election rival Yulia Tymoshenko and most of her party, Yanukovych pledged to steer a balanced line between Russia and Europe. His first trip abroad was not to Moscow, but to Brussels where he told EU leaders, "For Ukraine, European integration is a key priority of our foreign policy". His aim was also, he said: "Friendly and constructive relations with the Russian Federation and developing friendly relations with strategic partners such as the United States."[19]

The real change in relations would nevertheless be with Moscow, to where Yanukovych flew just three days after his visit to Brussels. "The new government in Ukraine will change relations with Russia, so that they will never again be like they were for the last five years," Yanukovych told Russian President Dmitri Medvedev. The Russian leader responded: "I hope that with your arrival and your work as president this black page in relations between Ukraine and the Russian Federation will be turned over, and we will see completely new conditions for cooperation."[20]

During his inauguration speech, in what would be viewed with bitter irony following his ignominious departure from office and from his country four years later, Yanukovych had made a pledge to combat corruption, in a country where this social and economic curse remained endemic.[21]

From the point of view of the EBRD, Yanukovych failed signally to deliver on his anti-corruption pledge. Towards the end of 2012, the Bank was becoming increasingly agitated about persistent reports of illegal raiding on businesses that were having a negative impact on business confidence. In internal meetings, management reported that public governance had continued to deteriorate and corruption had worsened significantly.

The EBRD was concerned that the Ukrainian administration had no real commitment to tackling this issue.

---

19 Stephen Castle, 'New leader of Ukraine seeks closer ties with E.U.' *International Herald Tribune*, 2 March 2010.

20 'Ukraine's Leader Visits Russia', *The New York Times,* 2 March 2010.

21 Mark Rachkevych, 'Ukraine's Yanukovych: corruption talks, EBRD walks', *Financial Times*, 6 November 2013, https://www.ft.com/content/664db72d-8ef5-386e-abb9-48948adcc6af.

In 2013, an expose from the openDemocracy website indicated that friends and family of the political leadership were the primary beneficiaries of the rent-seeking structures that dominated the Ukrainian political system and state.

An article, entitled 'Yanukovych's "Family" spreads its tentacles', referred to the President's recent political appointments, "all of which have gone to close associates of his elder son". Yanukovych was now dependent on his own inner circle, connected to him by the ties of "Family" business.[22]

Later, immediately after Yanukovych had been removed from office in 2014, Saakashvili, by then the former Georgian President revealed how the Ukrainian would openly boast to other heads of state how corrupt he was.

In an interview with the Guardian newspaper, Saakashvili said Yanukovych bragged at length about how his corrupt government worked, at a 2011 UN meeting in front of a group of leaders from post-Soviet countries. "He would talk very loudly about how he had corrupted senior officials, in the supreme court and the constitutional court," Saakashvili said. "He didn't care who he was talking to; the guy did not have any idea about morality."[23]

Anti-corruption efforts

Chakrabarti flew to Kyiv in February 2013 with a high-ranking management team for talks with the Ukrainian leadership where these concerns would be put firmly on the table. Reporting to the Board on his return, Chakrabarti said he had reinforced the EBRD's underlying commitment to investment in Ukraine, but this commitment would not come without strings attached.

The scale and the scope of future activities would depend on the government's success in securing macroeconomic stability, preferably through an IMF programme and by pushing further structural reform in certain sectors, particularly in the energy and local capital markets sectors. Crucially, the level of investment would depend on "seriously fighting corruption and unfair business practices".

---

22 Sergii Leshchenko, 'Ukraine: Yanukovych's "Family" spreads its tentacles', openDemocracy, 29 January 2013, https://www.opendemocracy.net/en/odr/ukraine-yanukovychs-family-spreads-its-tentacles/.

23 Shaun Walker, 'Viktor Yanukovych boasted of Ukraine corruption, says Mikheil Saakashvili', *The Guardian*, 25 February 2014, https://www.theguardian.com/world/2014/feb/25/viktor-yanukovych-ukraine-corruption-mikheil-saakashvili.

It was unusual for the EBRD to play out its political discussions with its countries of operations or its other shareholders in the public arena. Tough diplomatic messages had always tended to be confined to face-to-face, closed-door meetings. Open criticism of the Uzbek regime at the EBRD's Annual Meeting in Tashkent in 2003 led to an almost total freeze on EBRD activities in the country until after the death of Uzbekistan's long-term President Islam Karimov 13 years later.

In Ukraine, however, Chakrabarti was determined to go public and did not hold back in a news conference with international and local media. Just as Jean Lemierre had done in Tashkent, so Chakrabarti laid down a gauntlet to Yanukovych.

At the news briefing, the EBRD President said Ukraine needed to step up its fight against corruption to improve its deteriorating business climate. He spoke openly about the increasing number of complaints the EBRD had received from companies working in the country. Businesses had raised concerns about their treatment by tax and customs officials and courts. "The scope and scale of our investment will depend on the business climate," Chakrabarti said. "In recent months, as you all know, the business climate has deteriorated."

Businesses were complaining that tax authorities were trying to plug the growing budget deficit by forcing companies to make advance tax payments. Complaints about straightforward corruption were also common. Chakrabarti said: "We want to see much more action to tackle corruption at all levels. It is not just about passing laws, of course. Implementation is needed. We need concrete steps on these issues."[24]

The Ukrainian authorities—in public at least—responded positively to the EBRD's pressure. Yanukovych said Ukraine had been implementing reforms for over three years, and the country would hold to this course. He believed Ukraine should be given more time to implement these reforms, but he also stressed that Kyiv remained committed to closer ties with Europe: "Several things contribute to the effective cooperation between Ukraine and the EBRD. I mean, first of all, a stable partnership, in which the bank never lets Ukraine down, while Ukraine, its government, does its best to fulfil its obligations."[25]

---

24 'EBRD warns Ukraine over worsening business climate', *Reuters News*, 5 February 2013, https://www.reuters.com/article/ukraine-ebrd/ebrd-warns-ukraine-over-worsening-business-climate-idUSL5N0B5C1920130205.

25 'Yanukovych satisfied with Ukraine's cooperation with EBRD', *Interfax*, 5 February 2013.

One of the goals that the EBRD wanted to help Ukraine achieve at this time was getting into the top 100 countries of the World Bank's *Doing Business* ranking. It had crept up in the previous year to stand in the 137th position but it had much more work to do.

Just three days after the top-level meeting between the EBRD and Ukrainian presidents, concrete measures were made public that would support Ukraine's reform ambitions. One key element was the establishment, at the suggestion of the EBRD, of a business ombudsman that would aim to settle disputes between Ukrainian business and the authorities. Investors and other business people, both domestic and foreign, would be able to turn to the ombudsman to seek redress in response to their complaints.

The creation of the ombudsman was part of a larger anti-corruption initiative that the EBRD was developing, in conjunction—it was hoped—with the political leaders in Kyiv. In April, Chakrabarti told the *Wall Street Journal* that the EBRD was aiming to launch a plan to tackle corruption in Ukraine in the summer of 2013: "Until they do something about corruption, it's difficult to get foreign investors to go near the country."[26]

At the same time, the EU, while reporting progress on the creation of Association Agreements, including a Deep and Comprehensive Free Trade Area (DCFTA) with its eastern European neighbours in the Eastern Partnership (EaP), was also putting pressure on Kyiv. In order to proceed in Ukraine, the EU wanted to see further steps to make sure parliamentary elections were compliant with international standards, on addressing the issue of 'selective' justice and in implementing agreed reforms.

When Chakrabarti made a speech in Paris in June 2013 about the pervasive problem of corruption across the EBRD regions, he singled out Ukraine for a special mention. He also actively coaxed the Ukrainian authorities into action by pre-empting their own commitment to the EBRD's plans for the anti-corruption initiative. In a keynote speech to the Annual Anti-Corruption Conference of the International Bar Association, he said: "We are very pleased that the Ukrainian authorities have fully embraced the Initiative at the very highest political level and are determined to make it bite."[27]

But that confidence was misplaced as long as Yanukovych remained in charge in Kyiv. By November, there were clear signs of backtracking and

---

26 Paul Hannon, 'EBRD President Calls for "Radical" Steps to Boost Growth', *Wall Street Journal,* 29 April 2013.
27 EBRD Press release, 14 June 2013. 'EBRD steps up fight against corruption'.

Chakrabarti cancelled a trip to Kyiv after hearing that the Ukrainians were not ready to sign up to the initiative.

7. Yanukovych Suspends EU talks

Later in the month, the plans seemed back on again. But on 21 November 2013, Yanukovych dropped a political bombshell that would very quickly end his political career and change the face of Ukraine.

On 28 and 29 November, the third summit of the EU's Eastern Partnership was scheduled to be held in the Lithuanian capital of Vilnius, bringing together the heads of state or government from the 28 EU member states and the leaders of Armenia, Azerbaijan, Belarus, Georgia, Moldova and Ukraine. The partnership had been established in 2009 to reinforce the political association and economic integration of the six eastern European and south Caucasus partner countries.

EU Commission President José Manuel Barroso said the summit would deliver "change and a new perspective to citizens" of those six countries. It was, he said, part of a much bigger transformation taking place on the European Union's borders. "Ultimately Europe and the Eastern partners can only flourish as an integrated continent without dividing lines," Barroso said.[28]

The plan was for the EU to sign in Vilnius a far-reaching association and free trade agreement with Ukraine, as well as with Georgia and Moldova. The EU had been working hard to secure the accord, while at the same time prodding Ukraine ahead of the meeting to pursue legal reforms and work on human rights.

One particular pressure point was a call for the release from jail of the opposition leader, Tymoshenko, who had been imprisoned on what many in the West believed were trumped up political charges and who was seeking medical treatment in Germany.

At the same time, Moscow was making its own views clear about steps by Ukraine to move away from its sphere of influence, threatening retaliation and raising the spectre of a rerun of the "gas wars" between Moscow and Kyiv. In 2009, Russia had abruptly cut off the flow of gas through Ukraine

28 EC Press release, 26 November 2013. 'Third Eastern Partnership summit, Vilnius 28–29 November 2013,' https://ec.europa.eu/commission/presscorner/detail/en/IP_13_1169.

for 13 days, depriving much of south-eastern Europe of energy supplies during the height of winter. Similar action had been taken in 2006, with both sides blaming the other for the escalating tension.

Just as the EU had been courting Ukraine, Russia had been beckoning Ukraine to the Eurasian Economic Union, building on a customs union of Belarus, Kazakhstan and Russia that had been formed in 2010.

The pressure from Moscow proved irresistible and the hopes of the EU—and of an increasingly large number of Ukrainians—of forging closer ties were dramatically crushed when Yanukovych abruptly changed track. The Ukrainian government said on 21 November that the talks on a trade pact with the EU would be suspended and that it would pursue closer ties with Russia.

An order issued on the government website said Ukraine was suspending the "process of preparation" for the agreement "with the aim of adopting measures to ensure national (economic) security". It said Ukraine would "renew active dialogue" with Russia, other members of the (Moscow-led) customs union and the Commonwealth of Independent States with the aim of strengthening trade and economic links.[29]

Carl Bildt, who was Swedish Foreign Minister at the time, tweeted: "Ukraine government suddenly bows deeply to the Kremlin. Politics of brutal pressure evidently works."[30]

The Vilnius summit recorded the fact initially in typically neutral officialese: "The participants of the Vilnius Summit take note of the decision by the Ukrainian Government to suspend temporarily the process of preparations for signature of the Association Agreement and Deep and Comprehensive Free Trade Area between the EU and Ukraine."

The next sentence was less sanguine: "They also take note of the unprecedented public support for Ukraine's political association and economic integration with the EU."[31]

The reaction to the setback within Ukraine was as rapid as it was dramatic. The opposition said Yanukovych's failure to sign the deal was grounds for impeachment and called for the resignation of Prime Minister Azarov.

---

29 Richard Balmforth and Pavel Polityuk, 'Ukraine drops plan to go West, turns East to Moscow', *Reuters News*, 21 November 2013, https://www.reuters.com/article/us-ukraine-eu-idUSBRE9AK0S220131121.

30 @carlbildt, 21 November 2013, https://twitter.com/carlbildt/status/403521513342898176?s=20.

31 Council of the European Union, Joint Declaration of the Eastern Partnership Summit, Vilnius, 28–29 November 2013, https://www.consilium.europa.eu/media/31799/2013_eap-11-28-joint-declaration.pdf.

Putin's spokesman, Dmitry Peskov, said Russia welcomed Kyiv's desire to improve trade ties with Moscow, signalling satisfaction with a Ukrainian government decision to suspend preparations for the landmark trade pact.

EU foreign policy chief, Catherine Ashton, said in a statement: "This is a disappointment not just for the EU but, we believe, for the people of Ukraine."[32]

8. The Maidan Revolution and Annexation of Crimea

Ukrainians quickly responded. The following weekend, thousands of demonstrators took to the streets of Kyiv to protest against the government's decision to turn its back on the EU deal. The protestors staged a series of weekend demonstrations through the winter months that grew week by week in numbers, intensity and violence—climaxing in the 'Revolution of Dignity' that was played out primarily on *Maidan Nezalezhnosti*, or Independence Square.

Ten years earlier, the Maidan had been the focal point of the largely peaceful Orange Revolution that had pitched Tymoshenko and Yuschenko against Yanukovych and overturned his contested election victory. The 2014 revolution was anything but peaceful.

The months of protests across the country culminated in five days of conflict between 18 and 23 February that turned the Maidan into a battleground of smoke and fire. More than 100 protesters were killed, the victims now remembered as the 'Heavenly Hundred'.

Sevki Acuner was head of the EBRD's Ukraine operations at the time. He remembers the very fast eruption of extreme violence on the main city square. The previous couple of days had been relatively quiet. Acuner was living in his apartment, close to the centre of all the action:

> I remember the first shots. It was a calm and beautiful morning. When I woke up there was absolute silence. I heard one gunshot and then several gunshots and then all hell started breaking loose. I couldn't go out. I started watching the news on television of the snipers. I stuck my head

32 'EU says disappointed with Ukraine shift to the East', *Reuters*, 21 November 2013, https://uk.reuters.com/article/ukraine-eu-reaction/eu-says-disappointed-with-ukraine-shift-to-the-east-idUKL5N0J64HL20131121.

> out of the window to look and in that second a bomb went off. I pulled back in but there were dead people and people being shot on the corner of my street. It was a very shocking experience.[33]

An EU-mediated deal finally brought about a peace that saw Yanukovych removed from power, Tymoshenko released from jail and preparations for a new administration. By 23 February, Yanukovych had fled Kyiv, travelling ultimately to Russia, leaving behind a bruised nation, a trail of corruption and cronyism and a residential estate that was as opulent as it was tasteless.

Annexation of Crimea and sanctions

Significantly in the context of subsequent events, many of the largely ethnic Russian and Russian-speaking citizens in Crimea, who supported Yanukovych in the 2010 election, had condemned the protests in Kyiv. And very soon the peninsula itself was the scene of violence between those who supported the new post-Yanukovych interim Ukrainian administration and those who wanted to maintain close ties with Moscow.

In Sevastopol, opponents of the new government in Kyiv voted to establish a parallel administration in Crimea and pledged their allegiance to Putin. By 17 March, a referendum, declared illegal by the western powers, decided overwhelmingly in favour of a return of Crimea to Russia. The USA and the EU prepared to impose sanctions on Moscow.

The sanctions targeted Russian individuals, businesses and officials and Russia responded with tit-for-tat action, including a ban on food imports to Russia which had a direct impact on a number of EBRD countries of operations.

9. A Halt to Operations in Russia

New sanctions on Russia were on the agenda of a Special Meeting of EU leaders on 16 July 2014. According to the conclusions of the Council:

---

33 Interview, December 2020.

> The signature of new financing operations in the Russian Federation by the EIB will be suspended; member states will coordinate with the European Bank for Reconstruction and Development to adopt a similar position.[34]

The wording referring to the EIB and the EBRD differed, as the EU could not decide unilaterally to suspend EBRD financing to Russia, as it could in the case of the EIB, an entity solely controlled by the EU. The EBRD's unique shareholder structure took into account the concerns of all shareholders, which at the time comprised 64 countries as well as the EU and the EIB themselves.

However, it was clear that a sufficient number of Directors were in a position to deprive any project of the requisite majority needed to approve financing. As the statement issued by the Bank at the time said:

> A majority of Board of Directors of the European Bank for Reconstruction and Development (EBRD), including all EU member states and several non-EU shareholders, have given clear guidance to the EBRD management that, for the time being, they will be unable to approve new investment projects in the Russian Federation.[35]

Operational implications

EBRD management could not avoid becoming part of the sanctions, even if the EBRD's shareholder base and legal status precluded that.

It became an exercise in pragmatism. There was a large team in Russia—and not just in Moscow—backed by departments at the London headquarters who were dedicated to originating investments in the country. There would be no point in their determinedly pursuing viable transactions and preparing them for presentation through all the EBRD's internal vetting mechanisms, only for them to land in the boardroom and be rejected.

While no new projects would be presented, the EBRD would continue to manage its portfolio of existing projects and client relationships in Russia and it would maintain its physical presence in the country. It would also do whatever was necessary to protect existing investments.

---

34 Special meeting of the European Council, 16 July 2014, https://www.consilium.europa.eu/en/meetings/european-council/2014/07/16/.

35 EBRD Statement on operational approach in Russia, 23 July 2014.

In the first six months of 2014, Russia had accounted for just under one-fifth of the EBRD's total investments in the period of €3.6 billion—down from the heady heights of just a few years earlier but still a substantial share. Natasha Khanjenkova was managing director for Russia at the time of the new guidance on EBRD investment in the country. She and her team had been hoping that any action that might be taken would not prevent financing to the private sector. The news of the blanket ban came as a shock. Looking back, she said: "Uppermost in our minds was fulfilling the commitments we had to our clients and how we could remain a good partner, even if we weren't in a position to engage in new projects."

It was particularly important that, however disappointed clients were, relations between the business world and the EBRD remained strong. Khanjenkova added: "We tried to be as constructive as possible given the circumstances." The Bank continued to honour its obligations and disburse on signed contracts, as well as managing the existing portfolio.

Khanjenkova was reassured by the fact that the geopolitical tensions and the official rhetoric did not spill over into any problems or practical issues for the EBRD's operations in Russia or for its staff.

At its peak, the EBRD had a team of some 160 in Russia as a whole. Most of the staff—around 125—were in Moscow and the remainder spread across six regional offices outside Moscow spanning Russia's 11 time zones: Ekaterinburg, Krasnoyarsk, Rostov-on-Don, St Petersburg, Samara, and Vladivostok.

Many were needed to manage the still very large portfolio. Others were sector specialists who could apply their experience in other countries or be relocated there. Moscow was a very convenient hub for travel to other areas—especially Central Asia, the Caucasus or destinations like Belarus or Moldova. Khanjenkova was pleased with the results of the team effort: "One of the things I am most proud of is the way we were able to support our staff and to give them the opportunity to apply their skills and expertise in other countries of operations of the Bank."[36]

The regional offices were closed down in the coming years with the last one shutting in St Petersburg in August 2018. Towards the end of 2020, there were still some 45 staff in Russia in the Moscow office.

---

36 Interview, December 2020.

Tensions rise

If the relations for the EBRD in Russia remained as cordial as possible in the circumstances, the tensions rose on an institutional level.

Russia responded quickly to the EBRD statement. In a news conference in London, the day after the announcement, Russia's ambassador to the UK, Alexander Yakovenko, said Western sanctions against Moscow over its role in the crisis in Ukraine were "illegal, unreasonable and counterproductive". Yakovenko called the EBRD investment ban "unacceptable and harmful to all parties".[37]

Two days after new investment came to a stop, Chakrabarti was in Moscow for face-to-face meetings with the Russian authorities. The Economic Development Ministry issued a statement, reported in Russian media, quoting its minister Alexei Ulyukayev as telling the EBRD President that the financing halt contradicted the goals of international development institutions. He questioned the legitimacy of the steps taken at the EBRD and criticised what he called the political instrumentalisation of the institution. According to the reports, the statement said:

> For the last few months, Russia has repeatedly stated the inadmissibility of using the EBRD as an instrument of political pressure. Such actions are unconstructive and inconsistent with the goals of international development institutions. They can cause serious harm to the bank itself, clients, as well as the long-term interests of all its shareholders.[38]

The EBRD steadfastly separated the issue of its inability to pursue investments in Russia from the question of retaliatory EU measures, emphasising that the decision to halt new projects was not a matter of compliance with EU sanctions.

However, external comments in the media and even official comments from EU officials conflated the two. A statement issued by the European Commission on 29 July included a reference to the EBRD financing halt when it announced some additional measures targeting sectoral cooperation and exchanges with Russia:

---

37 'Russia's UK envoy: Western sanctions over Ukraine illegal and harmful', *Reuters News*, 24 July 2014.
38 'Russian economy ministry sees suspension of new EBRD projects as illegitimate', *Interfax*, 28 July 2014.

> This package reinforces the recently expanded listing of persons and entities undermining Ukrainian territorial integrity and sovereignty, including the so-called 'cronies', the suspension of EIB and EBRD financing, the restriction of investment and trade with Crimea and Sevastopol and the reassessment of the Russia EU bilateral cooperation with a view to reducing the level of the cooperation.[39]

Economic and financial consequences

The end to EBRD financing in Russia led a series of increasingly bitter attacks on the EBRD including threats of legal action—and a robust defence from the Bank itself.

There was no doubt that the sanctions overall had a significant impact on the Russian economy while the impact of the crisis was felt right across the EBRD's regions.

In an economic report published in September 2014, the Bank's economists were predicting stagnation for the Russian economy that year and a contraction in 2015. The Russian economy was under pressure, both from the sanctions imposed from abroad as well as from counter sanctions with which it had responded.

The escalation of military turbulence in eastern Ukraine was weighing heavily on Ukraine's economy and its external financing needs, with a sharp GDP contraction of 9 per cent forecast for the year. Against a backdrop of increasing military spending, Chief Economist Berglof referred to an erosion of the "peace dividend" from which the post-communist EBRD countries had been benefiting for close to 15 years. In its economic report, the EBRD said: "Permanently higher military spending in the transition region over the medium term, in response to the renewed geopolitical risks, could erode the peace dividend from the dissolution of the Soviet Union."[40]

The stagnating economy in Russia was bad news right across the EBRD's regions, affecting many of its neighbours that depended on growth there to support their own economies. Remittances from workers in Russia back to their families in Central Asia, the Caucasus and eastern Europe contracted

39 European Commission statement, 29 July 2014, https://ec.europa.eu/commission/presscorner/detail/en/STATEMENT_14_244.

40 EBRD Press release, 18 September 2014. 'Russia/Ukraine crisis casts shadow over emerging economies'.

in the first quarter of 2014 for the first time since the height of the global financial crisis in 2009.

The grim economic scenario took its toll on the EBRD's financial results—just as it had during the earlier global crisis. Amid the political backlash, a steep fall in the rouble depressed the value of the Bank's Russian equity stakes. At the same time, EBRD provisioning rose in response to the deteriorating economic performance of Ukraine.

The result was a net loss of €568 million, a substantial shortfall, even though it was largely on paper, and a significant swing from the 2013 net profit of €1.0 billion.

10. Russian Reactions

The Annual Meeting in Tbilisi

When Chakrabarti reported to the Board of Governors at the 2015 Annual Meeting in Tbilisi on the 2014 activities of the Bank, he said the disappointing operating environment was behind the losses, referring to the "impact of currency and market valuations of our Russian equity book and the deterioration in the quality of the Ukraine portfolio".[41]

For the Russian authorities, the Tbilisi meeting provided a very public platform upon which to vent their anger at the financing stop and to launch a sustained attack on what they perceived to be the failings of the EBRD's strategy.

In his remarks to the opening session of the Annual Meeting, the Russian Deputy Finance Minister Sergei Storchak blamed the losses on the financing suspension. The results "could partly be attributed to the Board of Directors' informal decision to suspend the Bank's operations in the Russian Federation," Storchak said. He added that in the view of the Russians, the action was politically motivated and totally lacking any economic rationale:

> We are surprised and disappointed that the EBRD, being a major and prestigious international financial institution, found itself involved in the sanctions polemics and was used to ramp up political and economic pressure on our country, which is contrary to the operating principles of

41 Opening speech to the Board of Governors, 2015 EBRD Annual Meeting.

> multilateral development banks and above all contradicts the mandate of the EBRD.

He complained that the EBRD had failed to deliver on goals set from the previous 2011–2015 planning period, in terms of operating assets, the size of the portfolio in the Bank's traditional region of operation, and its profit. He said agreements on the geographical distribution of investments had also not been observed.

What was more, Storchak said, the EBRD was now searching for new geographical and operational priorities, with business activity shifting to the new region for the Bank—the southern and eastern Mediterranean—and towards financing projects in Ukraine. It could not be said in every instance that the Bank's clients were observing the EBRD's strict internal rules and policies regarding projects' rates of return, the priority for investments into the private sector and the transparency of operations:

> It is essential that the EBRD remains a depoliticised transition institution. … We hope that the Bank will not be guided by temporary political trends, but will instead adhere to the basic principles of its operation stipulated in the Agreement Establishing the Bank.[42]

This became the standard tenor for Russian commentary about the EBRD for years to come, whether in the fortnightly Board meetings or in public arenas such as speeches or Annual Meetings.

Legal questions

Storchak continued in similar vein a year later at the 2016 Annual Meeting in London, referring to the adoption by the EBRD of a "political management" of Russian projects which he said was essentially an interpretation of the anti-Russian sanctions applied by some shareholders of the EBRD. He said the EBRD had in fact gone further than the EU and some other countries whose sanctions were aimed at Russian state companies and specific individuals.

Just two months later the Russian response was tightened a notch further, with a letter from the Russian authorities to the chairman of the

42 Russian delegate speech to 2015 EBRD Annual Meeting.

EBRD's Board of Governors which warned of potential legal steps aimed at challenging the guidance on Russian investments.

Russian media leapt on news of the letter from Alexei Ulyukayev, the Russian economy minister, to the Luxembourg finance minister Pierre Gramegna, interpreting the statement as a sign the Bank was going to be sued, even though the Bank's status precluded that possibility. In the letter, Ulyukayev wrote that Russia's representatives on the EBRD's Board of Directors "will shortly take legal steps … to restore the rights of the Russian Federation that have been infringed".[43]

The EBRD's Managing Director for Communications, Jonathan Charles, made clear in external comments to the media that there was no question of the Bank being sued, saying: "It is not about taking external legal action against the bank, it is about internal interpretation of EBRD procedures."[44]

At the EBRD's Annual Meeting in 2017 in Cyprus a line was drawn under the Russian charges, with a resolution put to Governors on whether the Bank had indeed abided by its own rules.

The Russian delegation came to the meeting fully equipped and determined to repeat the standard position. This time it was left to Russian Governor and Economy Minister Maxim Oreshkin to regret the "long-term unsustainability of the profitability of the Bank's operations", a "decline of the Bank's operational effectiveness", an "erosion of the Bank's operational mandate" and its "questionable risk management policies". Oreshkin concluded: "In the circumstances, having exhausted other ways of resolving the issue and to protect the interests of the Russian Federation as an EBRD shareholder and country of operations, Russia has no option but to take steps to identify a legal solution to the situation."

Oreshkin said the implementation of the "political guidance" violated legal norms, including the Agreement Establishing the Bank. He quoted widely from the AEB, including Article 8.3 on the possible suspension or modification of a member's access to EBRD resources: "Any decision on these matters must fall within the sole jurisdiction of the Board of Governors and may not be delegated to the Board of Directors."

43 Letter from the Governor for the Russian Federation to the Chair of the Board of Governors, Moscow, 5 July 2016.

44 Quoted in Buckley, 'Russia seeks to overturn EBRD lending ban', https://www.ft.com/content/f1fd3c5e-4462-11e6-b22f-79eb4891c97d.

In addition to other references to the AEB, he also cited Articles 32.2 and 32.3 on the international character of the Bank and the inadmissibility of attempts to exert influence over management in the interests of individual shareholders or groups of shareholders: "In essence, it amounts to discrimination based on nationality, and is inadmissible as part of the activities of a multilateral development institution."[45]

But when it came to a vote, the Governors exercising their powers under Article 57.2 of the AEB agreed overwhelmingly to support the view that the Bank had not violated its own rules in its dealings with Moscow.

Shareholders accounting for 96 per cent of its equity voted against the Russian challenge, with only Armenia, Belarus, Kyrgyz Republic and Mongolia understood to have sided with Moscow.

Chakrabarti said the Governors' decision was "final and binding" and there had been no discussion of what it would take to restart lending to Russia. Referring to the Governors' resolution, Chakrabarti nonetheless tried to offer some hopes for the future:

> However, I want to stress once again…that Russia is a member with which we have a special and deep relationship. The EBRD has continued to engage with Russia since July 2014, even though we have not been able to begin any new projects. Looking ahead, I want to continue to try to engage with the Russian authorities. As you know, we have a 25-year track record in the country, and I think that that should continue going forward. It is a very, very important relationship for me, for the Bank and for the region.[46]

Limbo continues

Six years later there was no change in the position of the shareholders, despite intermittent signals that some countries might be looking for a way out of the impasse. In March 2018, for example, Italy's ambassador to Moscow was quoted in an interview with Reuters as saying Italy would propose to other shareholders a resumption of lending in Russia to small- and medium-sized enterprises.[47]

---

45 Statement to the 2017 Annual Meeting by Maksim Oreshkin, Governor for the Russian Federation.

46 EBRD Press release, 16 May 2017. '2017 Annual Meeting, President's Closing Press Briefing'.

47 Katya Golubkova and Christian Lowe, 'Italy to propose EBRD resuming lending to SMEs in Russia – ambassador', *Reuters*, 8 March 2018, https://uk.reuters.com/article/uk-russia-italy-ebrd/italy-to-propose-ebrd-resuming-lending-to-smes-in-russia-ambassador-idUKKCN1GK1MU.

To the very end of his eight-year period in office, Chakrabarti would reflect regularly on the question—frequently posed by Russian media—whether the EBRD might resume lending to its once most important country of operations. His answer would be this was not a question for management but for shareholders and he saw little chance of any consensus developing for any change in the position.

Chakrabarti's hopes here as President of the EBRD did not come to pass. In the week he left the Bank in July 2020, he was quoted by the UK's *The Guardian* newspaper as saying there was "more chance of the organisation extending its operations to sub-Saharan Africa than of resuming lending to Russia".[48]

11. Ukraine after the Revolution of Dignity: A New Drive for Reform

In the wake of the overthrow of Yanukovych, the EBRD rapidly threw its weight behind the country once again, pledging publicly to step up funding as part of a coordinated programme of international assistance that would put Ukraine's reform programme back on track.

A statement released on 5 March 2014, said the EBRD was ready to provide investments of at least €5 billion over the period until 2020—and said that level could be higher depending on economic circumstances. It again stressed the need for Ukraine to make progress on corruption, and said it was looking forward to making real progress on the anti-corruption initiative that had been in the works for a year.[49]

It was putting support for reform at the heart of its activities in Ukraine. In many ways, the country became a test bed for Chakrabarti's increasing conviction that policy reforms and financial investment had to go hand in hand—right across the EBRD's regions.

Supporting reform and investing in Ukraine

The following day, 6 March, Chakrabarti issued a strong personal call to action, to help put Ukraine back on its feet with a public statement

---

48 Larry Elliott, 'Fifteen years after the G8 summit, it's the UK that's in dire need of aid', *Guardian,* 5 July 2020, https://www.theguardian.com/business/2020/jul/05/fifteen-years-after-gleneagles-its-the-uk-thats-in-need-of-aid.

49 EBRD Press release, 5 March 2014. 'EBRD statement on financing for Ukraine'.

proclaiming "Why we must support Ukraine". As the European Council in Brussels voiced its support for Ukraine that same day, stating "We stand by Ukraine",[50] Chakrabarti mapped out scaled up financing commitments by the EBRD and reform goals the Bank would pursue together with the Ukrainian authorities.

There was an urgent need for a shift in the economic policy mix to ensure sustainable development. Ukraine had to make clear there was no doubt in its commitment to the private sector. "For far too long, Ukraine had not used its resources efficiently and for a very narrow circle of beneficiaries only," Chakrabarti said.

Ukraine needed a radical break with the past, taking a cue from its western neighbours in building up small and medium-sized enterprises.

Most crucially, Ukraine needed the right institutional framework and a level playing field in order to allow its private sector to flourish. Good governance could no longer be overlooked. Now was the moment to make real progress on the business ombudsman proposals that Ukraine had failed to sign up to in 2013.

Chakrabarti was encouraged by the new administration's announcement that a purge of corruption would be a priority and he ensured the EBRD stood ready to contribute. The EBRD President put support for Ukraine in the context of the country becoming part of the European family, the very notion that had been so actively opposed by Russia and the dashed dreams of which had been the trigger for the weeks of protest that eventually ousted Yanukovych.

Restoring the rule of law to Ukraine was, he said, not only critical to restore order but to make the country attractive as a business destination again.

> It is also what it essentially means to be a part of Europe, a variety of nations with complex histories, shared values and a bright future. Ukraine has embarked on a new path. It is our duty to stand by this important country's side and we are ready to do so. Our help would be significant and we, together with the international community, are ready to deploy it, because we are all united in the determination that we want Ukraine to succeed.[51]

---

50 EC Press release: https://www.consilium.europa.eu/media/29285/141372.pdf.

51 EBRD Press release: Statement by Suma Chakrabarti, 6 March 2014. 'Why we must support Ukraine'.

Later in March, the EBRD lifted its restrictions on sovereign financing that had been in place since the previous year in response to the administration's refusal to take reforms and the fight against corruption seriously. This step allowed the Bank to announce a major investment in May into road transport infrastructure improvements.

The financing was delivered as part of a joint package with the EIB and the decision to proceed was made contingent on an IMF programme, underscoring just how firmly the EBRD's response to Ukraine was entrenched within a context of closer cooperation with other IFIs and development banks.[52]

It was Arseniy Yatsenyuk, the first Prime Minister after the ousting of Yanukovych, who launched the anti-corruption initiative with Chakrabarti at a ceremony in May in Kyiv.

A former economy and then foreign minister in the 2000s, Yatsenyuk had famously become the centre of a controversial leaked conversation between senior US state department official Victoria Nuland and the US ambassador to Ukraine Geoffrey Pyatt as they discussed who they thought should take senior roles in any new administration. In the conversation, Nuland was heard to back Yatsenyuk, saying: "I think Yats is the guy who's got the economic experience, the governing experience."[53]

Yatsenyuk held the position for two years.

At the launch of the anti-corruption drive, attended by Yatsenyuk, Chakrabarti praised the new administration's commitment to taking on the challenges. He described corruption as a scourge, "hollowing out the economy, eating away at political life and undermining democracy". Chakrabarti noted that signing the memorandum and launching this initiative would not stop corruption but, he added: "We salute the government of Ukraine for its determination to tackle this fundamental problem regardless of the adverse geopolitical situation in the country."[54]

The EBRD turned to a number of national governments to secure financing to help promote policy reform across the country. Grant money from the EBRD's Stabilisation and Sustainable Growth Multi-Donor Account (MDA) Fund was quickly applied to financing the administration of the

52 EBRD Press release, 6 May, 2014. 'EBRD steps up lending to Ukraine as part of international support package'.

53 'Ukraine crisis: Transcript of leaked Nuland-Pyatt call', *BBC News*, 7 February 2014, https://www.bbc.co.uk/news/world-europe-26079957.

54 EBRD Press release, 12 May 2014. 'Ukraine and EBRD launch initiative to combat corruption'.

office of the new business ombudsman that had been created as part of the anti-corruption initiative. Former Lithuanian Finance Minister and EU Commissioner Algirdas Šemeta took up the role of business ombudsman towards the end of the year.[55]

The EBRD closed the year with a 50 per cent increase in investments to Ukraine in 2014 to €1.2 billion and underlined this renewed commitment with the opening of a second office in the country, in the western city of Lviv, where an emphasis would be placed especially on support for small and medium-sized business in that region. Two years later it would expand eastwards with a second regional office outside Kyiv in Kharkiv.

In eastern Ukraine in early 2015, however, war was still raging between Ukrainian government forces and Russian-backed separatists who had declared 'people's republics' in the disputed region. The nine-month long conflict that erupted after Russia's annexation of Crimea had claimed the lives of over 5,000 people.

Peace talks built around the Minsk Protocol, devised in the Belarusian capital three months earlier and bringing together Ukraine, Russia and the Organisation for Security and Cooperation in Europe (OSCE), collapsed at the end of January 2016. The violence continued and there was still no peace six years after the initial outbreak of fighting.

The timing for making real progress on reforms was not propitious, with the new administration under President Petro Poroshenko having to focus on an increasingly bitter and costly war. But progress was indeed made with a government that Chakrabarti was to call later that year "one of the most professional administrations that we in the EBRD have ever worked with".[56]

The EBRD had already been an important backer, with financial support from its MDA fund, of Ukraine's National Reforms Council. The Council, founded in December 2014, created a platform for political consensus-building around key national reforms, stretching across all departments of government with the aim of making coordination of the reform process more systematic.

---

55 EBRD Press release, 3 November 2014. 'EBRD establishes multi-donor fund to support reforms in Ukraine'.

56 EBRD Press release: Speech transcript, 9 June 2015. 'The way forward for Ukraine'.

The Ukraine Reform Architecture project

Later the EBRD, jointly with the EU, would embark on an even more ambitious plan, a ground-breaking and transformational state-building project that aimed to put in place a new home-grown generation of professional and highly qualified reform experts—dubbed "local change agents"—to drive the transformation needed from the inside.

This Ukraine Reform Architecture (URA) project, launched in 2016, was built around the concept of embedding reform-minded Ukrainians in ministries within the Ukrainian government.

Bojana Reiner, a Senior Governance Counsellor at the EBRD, who helped design and implement the project described it as "a gene therapy for the state". The local element—local doers and change agents—was a crucial part of the programme, ensuring that Ukrainians themselves had ownership of dealing with the challenges. It was not just a top-down exercise where foreign experts would come in and dispense wisdom. Reiner said: "It was innovation in state design, built around three core principles: local genes for local problems; incubate then integrate; and experiment, learn, adapt."[57]

A vital aspect of the programme was to make sure civil servants were adequately compensated, reducing the temptation of seeking financial backhanders for favours and helping to eradicate corruption. It also stayed away from the typical recipe of paying fees at 'western' consultant levels since these costs were unsustainable on a large scale. Instead, a new pay grade was designed that would afford a decent living in Ukraine, comparable to other countries, but which did not alienate those working there already.

Among the many projects rolled out to promote the reform process in Ukraine, two stand out particularly: one in the energy sector and another in banking.

Naftogaz

A combination of financial investment and efforts to raise business standards and drive forward reforms was applied to the Ukrainian gas industry, long seen as a quagmire of inefficiency and corruption. This was much more than the simple provision of finance for infrastructure projects.

57 Interview, December 2020.

The investments sought to transform the quality of governance at the two companies that were at the heart of the Ukrainian gas industry: NJSC Naftogaz, the national oil and gas holding company, and its subsidiary, Ukrtransgaz, which operated pipelines and storage facilities. Negotiations to deliver these investments took place at the highest levels of the Ukrainian administration, with the clear intent of ensuring strong government backing.

According to Francis Malige, then EBRD Managing Director for Eastern Europe and the Caucasus, and based in Kyiv: "The transformation of Naftogaz was a litmus test for the government's resolve to reform in those years. The company was one of the darkest corners of the country's web of corrupt interest."[58]

The EBRD was a driving force behind the reforms that were at the very heart of this project. "Working with the government and the company's new management, we designed a structure that would create and sustain the incentive to reform."

The EBRD took on the problems of the Ukrainian gas industry with a package of two closely intertwined investments: a long-term loan to refurbish the most critical sections of the main transit pipeline, and a short-term loan to finance winter gas purchases at a time when access to foreign financing was problematic for Ukraine.

The short-term loan was re-issued every year, coinciding with important transformation milestones and making sure that the reform process maintained momentum. The long-term loan was a €150 million credit to Uktransgaz to allow it to carry out crucial upgrades to the key energy transit facility, the Urengoy-Pomary-Uzhgorod pipeline.

The pipeline transported Russian gas to European markets and also provided for reverse gas flows from the EU back into Ukraine. The modernisation of the pipeline was an important step in increasing energy efficiency in the industry, reducing the perennial problem of gas leakage during the transit process.

Most crucially, the EBRD's loan came with a series of conditions that would improve corporate governance of both Ukrtransgaz and its Naftogaz parent and contribute to the overall transparency of Ukraine's energy sector.[59] It was important too that links were made to IMF programmes and

58 Interview, December 2020.

59 See Chapter 8.

advice and that the Ukrainian government committed to reforms aimed a delivering best practice in the development of market-based principles and liberalisation of the sector.

When the EBRD signed its US$ 300 million loan agreement with Ukraine to finance gas purchases over the following winter, it was amid much fanfare at a ceremony in Berlin attended by German Chancellor Angela Merkel and Ukrainian Prime Minister Yatsenyuk. The EBRD funding allowed Ukraine to buy up over 1 billion cubic metres of gas that would fill its storage facilities ahead of the winter.

The loan would not just provide a short-term response that would tide Ukraine over possible energy shortages over the coming months. It was part of longer-term efforts by the international community to strengthen Ukraine's energy security by supporting diversification of suppliers and delivery routes. And, again, at its core was the EBRD's commitment to driving forward the reform process in Ukraine.

The loan was conditional upon a programme of corporate restructuring at Naftogaz. This included the creation of a supervisory board of independent and qualified directors. Naftogaz would have to introduce internal audit, compliance, anti-corruption and risk management functions and an ownership and governance structure in line with best international practice.

In any country where reforms are introduced there is opposition, especially from those with a vested interest in maintaining the status quo. By its very definition, the creation of a level playing field implies taking something away from one quarter and sharing it with another. The reform proposals for Naftogaz were no exception.

Even when Malige was asked by Yatseniuk to present the project to his entire cabinet—in itself a signal of the EBRD's role in delivering real change at the heart of the administration—there were murmurings of dissent:

> Before the cabinet meeting, I was taken aside by Yatseniuk for a brief discussion with the EU ambassador, and the ministers of economy and finance. The ministers both said their own departments had come up with objections. But they both said they knew this was the right thing to do for the sake of the country.

Yatseniuk was then happy to proceed.

> We moved from the ante-room into the ornate grandeur of the cabinet meeting room. I then presented the whole EBRD concept to the assembled ministers, assuaging any further concerns and making sure the project was finally delivered.

PrivatBank

The other standout intervention during this period was the decision by the EBRD to support and encourage the Ukrainian authorities with the nationalisation of the country's largest bank, PrivatBank, after the discovery of a US$ 5.5 billion hole in its balance sheet.

Control of the bank was taken away from its oligarch majority co-owners Igor Kolomoisky and Gennady Bogolubov. Announcing the decision in a televised news conference, National Bank of Ukraine Governor Valeria Gontareva said PrivatBank had been undermined by widescale lending to entities close to the owners.

Kolomoisky has consistently denied any wrongdoing and continued to reject the way the central bank characterised the state of PrivatBank's finances at the time of the nationalisation.

This was the latest in a series of steps under Gontareva to clean up the banking sector, including closing down over 80 of the country's 180 banks. Many of these banks had been purely used for money laundering. Others were called "zombie banks" by the central bank chief, and had only liabilities and no assets, while a third category, she said, were used just for the benefit of investment in the business of their owners.

The EBRD was very vocal in its support for the nationalisation, on the face of it not the typical economic stance from an institution with a mandate to promote the private sector and which had spent decades helping to transfer assets away from the public sector.

It chimed very clearly, however, with the EBRD's view that the private sector could only flourish against a backdrop of good governance. In a statement, Chakrabarti said:

> The long-term stability of PrivatBank ... is crucial to the country's economic health. We believe the decision to nationalise it is the right one and have offered our expertise to the authorities whenever it is needed. We strongly

> support the National Bank's continuing efforts to reform the banking system in Ukraine and ensure good governance across the industry.[60]

Malige was in close touch with the authorities in the run-up to the nationalisation. He subsequently became a non-executive member of PrivatBank's supervisory board. Appointed later as managing director for financial institutions at the EBRD, Malige has no doubt that the EBRD's support for the nationalisation and its backing for other reforms in Ukraine was the right step to take:

> I would do it again. There is no way the country would have progressed so far without the support, from the EBRD and the coalition of IFIs, the US, the EU and other countries such as France, Italy, Canada, that we put together. It was this backing that helped improve the standard of governance at Naftogaz. Without this support, would they have dared to have closed down so many banks and nationalised PrivatBank? I don't think so.

But he stressed emphatically that the real heavy lifting at this time was done by the Ukrainians themselves:

> The reform of the banking system was certainly driven by the Ukrainians. We have to pay homage to the courage and determination of the Ukrainian people who did it and who paid a price for it.

One of those people was Gontareva herself, who left the National Bank in 2017, and who later said she feared for her life after becoming a victim of intimidation and harassment. She was injured when a car drove into her in central London and then her son's car was torched in Kyiv. Her house was later burnt down in an arson attack.

Malige said the creation of the ombudsman and the EBRD's anti-corruption initiative were important steps for Ukraine. The ombudsman was clearly a great success. Many companies were now able to resist the demands of corrupt officials. And the support for bank reform also meant that many banks were no longer conduits for corrupt money.

60 EBRD Press statement, 18 April 2019. 'EBRD statement on PrivatBank'.

Speaking in 2020, he made clear there was still more work to be done. There had been clear determination to tackle the problem. But laws that had been made had to be implemented. "The biggest issue in Ukraine is and unfortunately will continue to be the weak rule of law and the high level of corruption."

Part II

Towards Sustainable Market Economies

Chapter 6

Rethinking Transition

Introduction

The global financial crisis came as a profound shock to the international financial community. After a period of success for the EBRD and its countries of operations the effects were devastating as economic growth slammed into reverse. There had been serious disruption in many transition countries a decade earlier when the Russian crisis hit. But then a swift recovery followed. This time the downturn was deeper, more widespread and prolonged.[1] Whereas the Russia crisis had dented the transition process, this time it was under much more serious threat.

As unemployment rose and banks deleveraged, and as growth prospects diminished, the boardrooms of corporates that had invested in the east heard executives no longer asking "How do we get in?" but "How do we get out?". The world of transition appeared to have been turned on its head. Gains from the convergence of economic systems no longer looked a sure-fire bet.

Dissatisfaction grew. Transition was not at fault per se but it did not seem to be helping. In 2010, less than one-half of respondents to a large survey of the EBRD region expressed satisfaction with their lives compared with almost three-quarters of those surveyed in western Europe. Two-thirds of households in transition countries had suffered as a result of the crisis, through lost jobs, reduced wages and remittances; and a large proportion were compelled to reduce their consumption of basic necessities. The harder the impact of the

1 GDP growth in Russia fell from 1.4 per cent in 1997 to -5.3 per cent in 1998 before recovering the next year, while growth in CEB remained steady in these years at 2.4 per cent and 2.7 per cent, respectively (and again the following year with growth of 2.0 per cent).

crisis, the lower the satisfaction level. Overall, in more than half the EBRD countries surveyed respondents felt the position had worsened since 2006.[2]

The same survey showed support for markets and democracy also fell significantly in more advanced transition countries as a result of the crisis. Trust in banks, financial institutions and foreign investors fell. The more citizens were personally affected by the crisis the more they turned away from democracy and the free market.[3]

Doubts had been sown by the experience of financial failure. But an even longer-standing and pernicious problem was that of corruption. This was perceived to be worse than before the start of the transition and deteriorating rather than improving. The general level of trust in society was also low. The path ahead was no longer clear.

The severe consequences of the great recession called into question the robustness of transition and the model on which it had been built. Western investment and support, including by the EBRD, had undoubtedly been valuable in kick-starting a moribund economic system and leading it towards a more successful, market-oriented economy. But now that the tide of market exuberance had turned and been replaced by market adjustment and economic hardship, the value of markets and liberalisation were being called into question.

The EBRD itself was not immune from this self-examination. A previously implicit presumption of a more or less linear transformation from planned to market economy and from communism to democracy looked at odds with the facts. A turning away from the EBRD founders' belief in market democracy had already been seen in Russia after its crisis. It was now apparent that a similar course could occur elsewhere in the region. The risk of transition reversals in countries of operations became a major topic of conversation.

This was the context for the start of a rethink within the EBRD about transition. Drawing on academic developments and its experience in the field and the world of finance, management embarked on a major reconsideration of the concept underlying transition and its application to the Bank's operational activities.

Over the next decade this rethink allowed the EBRD to remodel itself and establish a firmer base for delivery of its transition mandate. It became

2 *Life in Transition*, *Survey II*, 2010.
3 'The Intangible Transition', Chapter 3, 'Crisis and Transition', *Transition Report 2011*.

based on a revised view of what was needed for the transition to a *sustainable* market economy, one that could survive the vagaries of market turbulence, drawbacks and inequities, and adapt to democratic pressures.

The changes made also helped to remove the sense of an anachronistic organisation tied to the past, and placed the EBRD at the forefront of MDB actions to meet development needs by transforming markets to support private sector development. The EBRD successfully partnered with private sector and other players to leverage funds for global public goals, such as tackling climate change and improving equality of opportunities for people.

1. Methodological Strains

The internal strains that emerged over the EBRD's future from the debate on graduation in the early 2000s partially eased over time as a new geography opened up to the Bank's realm of operations.[4] The philosophical debate as to whether the Bank was there solely to help former communist countries develop a market and democratic orientation became resolved. The EBRD's remit could be applied to a wider group of countries, at least within the European arena, though the issue of winding down activities in more advanced countries remained.

Strains arising during the same period over the understanding of the ultimate goals of transition did not diminish, however. What exactly did an open, market-oriented economy involve? Was demonopolisation and privatisation of state assets, or the putting in place of western market structures, sufficient for successful transition? And what else might be needed to ensure that countries would continue to evolve in an open, competitive, market-based and democratic manner?

The pressures to curb business in some countries from ideas on graduation and differing interpretations of transition renewed tensions within the Bank between economists and bankers. This was exacerbated by the economists' major influence over project approvals. That influence was exerted through their management of an independent project scoring system whose

4 Described in Part I. See also Kilpatrick, *After the Berlin Wall*, Chapter 12.

scores and transition impact assessments fed into project documents seen by the Board and into the Bank's annual corporate performance scorecard.[5]

By the mid-2000s, after more than 15 years of studying and assessing transition, the EBRD's economists were pleased with the transition impact assessment system that was by now deeply embedded in the operational mechanics of the Bank. But, even though the prospect of Turkey as a new country of operations boosted hopes for business, bankers faced practical uncertainties from the pressures to shift business away from EU countries expected to graduate by the end of the decade. They began to take aim at perceived constraints to the growth of their operations. Among them was the methodology that applied to the transition assessment of projects.

In several areas—for example, projects with repeat clients and debates over outcomes versus structures—there were increasingly heated arguments between bankers and economists. One big issue concerned conflict of interest, with bankers influenced by the interests of their clients rather than the public interest in a competitive playing field.

Then, as a new stream of business in sustainable energy expanded in the second half of the decade, environmentalists joined in pushing back against the economists who saw themselves as guardians of the EBRD's mandate. The Bank's senior management looked to the transition architects in the Office of the Chief Economist (OCE) for solutions, hoping that peace might break out before long.

Responding to the challenge, Erik Berglof, as Chief Economist, and Hans Peter Lankes as his deputy began to tackle questions the bankers had raised. The main disputes were clustered around three areas: repeat clients and critical mass;[6] the role of state enterprises; and environmental and gender issues.

Repeat clients and critical mass

In most countries in the EBRD region, the number of well-established local corporate players and influential financial institutions was small. The Bank had helped to establish many of them. As a result, the bankers knew these

5 See Kilpatrick, *After the Berlin Wall*, Chapter 10 for a description of the evolution of the project assessment system and later in this chapter for further developments.

6 The notion that the sum of a large number of projects can have a wider effect than the sum of their parts and lead to a "take-off" point for wider, self-sustaining diffusion of the technologies or products behind them.

clients very well, having spent years building up relationships with them, and often used them to branch out into new business areas.

However, some projects were simply replicas of earlier investments: for example, repeated lines of credit for working capital for the new grain harvest, investment in a second turbine at a power plant, extension of a processing plant or production line, a further credit line for on-lending to SMEs to the same bank, and so on.

Viewed from the perspective of systemic change—a key objective of transition—these types of project won little favour from the economists in charge of rating bankers' projects for their transition impact. Unless a radical new process or management change was introduced, the incremental systemic value of similar projects was low. The economists' preference was thus for projects with new clients and new business areas where the boundaries of the market might be broadened. But this was more difficult for bankers to engineer.

The economists were also concerned about additionality, the notion that projects would not otherwise happen without the EBRD's intervention, especially in more mature market areas.

In earlier days this was an intermittent problem, but the cumulation and growth of EBRD operations led to more frequent repeat projects with well-established clients where it became harder to argue they had no market access. The speed with which bankers found new clients or activities did not match that of investment volumes, so repeat business with the same clients increased, and with it clashes with tests of systemic impact and additionality.

This was not an easy problem on which to reach agreement. Hints were given on the idea of accepting a combination of repeat projects where a critical mass effect might apply and the use of investment frameworks, which badged similar projects under one umbrella, helped to ease the tensions a little. But it was only later that packaging a combination of investments, technical assistance and policy advice under integrated approaches provided a more promising solution.

Public infrastructure and state-owned enterprises

The Banking Department and OCE were also often at loggerheads over infrastructure projects financed with sovereign or sovereign-guaranteed loans.

In many less advanced transition countries, infrastructure needs were large and a primary source of business for the EBRD. There was no doubt that

such investments were needed. Bankers pointed out that the private sector could hardly thrive where power supplies were constantly interrupted, roads were barely passable and docks lacked the capacity to process container ships. In principle, such projects met a basic requirement laid down in the Articles of the Agreement Establishing the Bank (AEB) to allow public infrastructure investment where it was deemed "necessary for private sector development".

But the economists argued that supporting state-owned institutions per se did not foster competitive market-oriented solutions in line with the Bank's rationale. For them, more was needed: either investment in a state-owned enterprise on a path towards commercialisation and privatisation or improvements to regulation and legal requirements which would eventually permit private sector participation. Where these routes were missing bankers first had to engage intensively with the authorities in policy discussions.

Policy advice was not something the average private sector investment banker expected to undertake or was trained to do, and it was especially difficult in countries where administrative capacity was weak. It took time to develop policy capacity within the Bank and time-consuming efforts with authorities to find ways of making such investments work satisfactorily. Bankers baulked at the idea that a US$ 100 million loan for, say, a new turbine generator which would increase reliable electricity supplies might be blocked by the economists without a parallel dialogue on tariff setting, dispatch rules or the establishment of an independent regulator.

Nonetheless, as senior bankers gained knowledge and experience of the local conditions and as the Bank pushed further into less advanced countries, policy became a more accepted activity by bankers in infrastructure projects and better integrated with the investment process. Importantly, they were helped by lawyers in the Bank, especially from the Legal Transition team, and by advisory staff and consultants employed through technical assistance contracts.

Internally, however, tensions with economists exploded from time to time over the extent of policy inputs required. Agreement was needed on a better way forward than a series of lengthy negotiations and ad hoc solutions.

Environmental and social issues

Another area of concern was environmental and social standards. For many years, the environmental experts in the Bank had argued that projects which

cleaned up the environment, such as reducing pollution in the Neva Basin near St Petersburg, were in line with the Bank's purpose (under Article 2). The economists accepted their environmental value, but not as a source of systemic impact in relation to the transition towards a competitive, market economy.

Similarly, social standards, including gender, were seen as outside the economic perspective taken on transition impact.

This led to a growing tension between the focus on environment and transition impact. The obvious metrics for establishing impact in environmental projects were outcomes, such as the amount of pollutants reduced or carbon saved. This was something shareholders and donors understood. Measures of transition impact, on the other hand, looked mainly at intermediate goals towards market development, such as the dissemination of a new process or introduction of an energy management system, and tended to be more complex and difficult to aggregate across different projects. The emphasis on the approach taken (a new energy management system), rather than outcomes (reduction in emissions), made it harder for the economists to explain their position.

As the Bank geared up its efforts on sustainable energy (see Chapter 9) dissent grew over the value of improvements in energy use, particularly in repeat projects and public utilities, where CO_2 was reduced even if there was no apparent systemic market effect.[7] Bankers and environmentalists argued that the value of the project to the environment was being ignored or discounted. If an investment in a new combined cycle gas turbine public entity increased efficiency and reduced CO_2 emissions surely the operation met the Bank's mandate, even if the market structure was unchanged? Was another line of credit to a bank for on-lending to SMEs for energy efficiency purposes not as valuable in its impact as the first one?

Berglof and Lankes responded to these concerns with a paper issued in April 2008 that linked environmental considerations more closely to the transition methodology.[8] It introduced the notion of "strategic fit" in the context of efforts to achieve aggregate transition impact, for example through a comprehensive programme of projects, policy dialogue and

7 Improvements to street lighting was one such contentious example, or energy efficiency improvements to public buildings.

8 'Considering Environmental and Sustainability Objectives in Assessing Project Transition Impact', 14 April 2008.

technical assistance targeting sustainable environmental improvements.[9] The idea was to maintain the project-level impact assessment, but add the environmental dimension at a programmatic level and allow the monitoring of outcomes to be conducted there. This later became generalised into an 'integrated approach'.

Workarounds to broker solutions and accommodate particular cases only worked so far, however. The system continued to be seen as complicated and lacking transparency. Bankers hankered after a simple, easy-to-understand judgement on the transition value of their projects. More holistic solutions were needed. Then the financial crisis intervened.

2. Balancing Markets and the State

The crisis forced a fundamental rethink within the EBRD: about its role, past misconceptions and mistakes over transition and how to operationalise its mandate in the post-crisis environment. Already by early 2009, the Bank's management began a process of reflection on the implications of the crisis for the transition process and what the EBRD should look out for and where it could do better.[10]

Management was also conscious of the first *Life in Transition Survey* (LITS) in 2006 which showed that even when growth had been good people in transition countries were not yet convinced their lives were changing for the better. With a low degree of trust and two-thirds of respondents saying corruption was as bad or worse than before the transition began some

9 An Index of Sustainable Energy was constructed to help. This was based on three equal components measuring energy efficiency, renewable energy and climate change. Within each, there were measures of the quality of relevant institutions and policies (e.g., laws, regulatory policies, project implementation capacity); market incentives such as pricing, methods to generate energy savings, support for renewables and market-based mechanisms for climate change mitigation; and outcomes such as energy and carbon intensity and use of renewables compared with global benchmarks. The index showed Slovenia, Lithuania, and Hungary as the top three performers (closely followed by several other EU countries), with the Kyrgyz Republic, Turkmenistan and Tajikistan the worst performers.

10 One immediate development concerned whether repeated finance to existing clients via short-term or working capital lines, or refinancing operations to help stave off bankruptcy in the crisis environment, might count as transition impact. This was proposed on the basis of preserving existing transition achievements—where previously strong or impact-minded companies were at risk of going under—but without advancing transition as had been required in previous assessments. Flexibility in interpretation was adopted by taking a view of the probable counterfactual to decide the extent of the likely transition reversal, something that could only be done on a case-by-case basis.

deeper aspects of the transition picture were particularly worrying.[11] A similar survey was planned for 2010, with the effects of the recession expected to reveal further problematic results.[12]

Deepening transition: The 2010 capital resource review

The timing of the rethink coincided with the run-up to the next five-year corporate strategy planning period for 2011–2015, Capital Resource Review 4 (CRR4), due to be signed off by Governors at the Annual Meeting in Zagreb in 2010. As well as work to support a gearing-up of the EBRD's business volume as part of its counter-cyclical response (see Chapter 2), there was an effort to learn lessons from the crisis and how the path of transition had been evolving beforehand.

An important preliminary paper, 'Fighting the Crisis, Promoting Recovery and Deepening Transition', had been sent to Governors in April 2009 ahead of the May Annual Meeting in London. In his covering letter, Thomas Mirow pointed to the region's vulnerabilities—a strong dependence on capital inflows, high levels of foreign currency denominated debt and in some cases excessive reliance on commodities[13]—and the risk that important transition achievements could be reversed. He envisaged a need to improve the "quality of both public and private institutions" and ensure that they worked well together.

The paper took up this theme in more detail: "Our understanding of the transition process and the Bank itself have evolved [and] given rise to a careful reassessment of ... the meaning of transition itself [and, in particular,] an even stronger focus on the quality of institutions."

---

11 LITS I surveyed 29,000 people in 2006 across the Bank's regions. Only 30 per cent believed that their "household lives better today than in 1989", although they were more optimistic about the future. A particularly striking finding was that less than 15 per cent of respondents thought there was less corruption than in 1989 and two-thirds believed it was as bad or had increased since the transition began. The view on whether people could generally be trusted was very low. Less than one third of respondents in 2006 believed people could generally be trusted compared with two-thirds holding these views of the period before 1989.

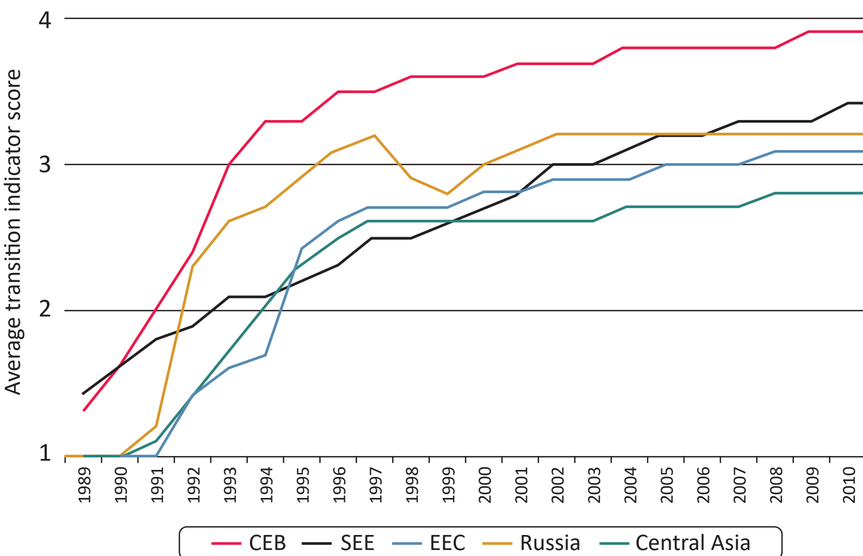
12 Management fears were indeed borne out by the LITS II survey which showed widespread suffering as a result of the crisis and continuing dissatisfaction and distrust, as described in the introduction to this chapter. See 'Life in Transition: After the crisis', *Life in Transition Survey II*, EBRD, 29 June 2011.

13 Although this referred to a lack of diversification, one vulnerability of concern at the time that is less remembered today came from the food price crisis of 2007-8 which had a significant impact on several EBRD countries of operations where food costs formed a high percentage of household expenditures. These were estimated at more than 50 per cent in Ukraine, for example, and over 40 per cent in Romania and Moldova, according to LITS I.

It was the case, nonetheless, that "vast improvements" had been achieved over 20 years of transition, in terms of resource allocation and economic performance. The EBRD had been established at a time when there were severe limits to market development, entrepreneurship and democracy in its region: "Transition was about reducing direct state intervention in the economy and establishing some basic market mechanisms."

This path of advancement could be seen in the EBRD Transition Indicator scores, published annually in the *Transition Report*. These showed progress towards levels equivalent to an advanced industrial economy (a score of 4.3) based on an array of indicators relating to privatisation, market liberalisation, trade and financial development.[14] As Figure 6.1 illustrates, significant progress was made against these yardsticks in the 1990s, although the rate differed across the region. Countries further away from central Europe tended to make fewer gains, and by the turn of the millennium CIS countries were lagging behind.

Figure 6.1 Transition Indicator Scores, 1990–2010



14 For more details, see Kilpatrick, *After the Berlin Wall*, Chapter 10, pp. 270–274.

But it was clear from the early 2000s on that the pace of progress had showed. Even before the crisis the next stage of transition was proving harder to reach. And, when the crisis came, even central Europe and the Baltics, where most second-stage reforms were in place, suffered serious setbacks—and their economic performance disproportionately so compared with their western European counterparts. Questions were raised, as emphasised by the title to the 2009 *Transition Report* published that November, '*Transition in Crisis?*'.

The final paper for Governors made clear that the consequences for transition and the model on which it had been built might be serious:

> The most important impact of the crisis may be political ... Questions about the market and globalisation are being asked ... [and] may erode confidence in the model that the transition countries have been encouraged to follow for the past 20 years.

While in the early years of the Bank it had been right to pursue "less state and more market" it was now important to recognise:

> Transition is not just about the *size* of the state's footprint in the economy, but about where and how the state treads: that is, *what* the state does to affect economic outcomes, and *how* it attempts to do so.

The implication was that the quality aspects of transition were as essential as the presence of a private sector. This applied to state interventions, such as enforcing laws or collecting taxes, as well as to non-state interventions since markets could not function well if there were barriers to entry or poor corporate governance for instance. "The state and private institutions generally are not substitutes", the paper said:

> Transition is about building markets and the private sector, but it is also about redefining the state as opposed to minimising it ...Going forward, the emphasis on quality—private and state—is perhaps the most fundamental challenge for transition.

The Besley Commission

The financial crisis was a trigger for Berglof to put into play an idea he had been considering for some time. He was well aware of developments in academic economic thinking, especially the role of institutions in shaping economies and markets, and decided the time had come to incorporate some of these ideas in the EBRD context. Academics could provide an external view of the transition assessment methodology, and its tools, as well as on some of the issues that had arisen with Banking.

Berglof knew Professor Tim Besley at the London School of Economics (LSE) well and contacted him to see if he would chair a panel of experts to consider the issues. Besley, a policy expert on development economics and political economy, agreed and was joined in the task by two other distinguished economists: Matthias Dewatripont, professor at Université Libre de Bruxelles, a specialist in contract theory, incentives and industrial organisation, and Sergei Guriev,[15] then Professor and Rector at the New Economic School in Moscow, whose knowledge of the economics of development and transition and corporate governance completed the team.

The group was asked to look at the transition concept in the context of a broader discussion of development and institutional change and consider the appropriateness of the methodology used to assess transition progress and the Bank's operations. This was to be done with reference both to academic work and interviews with staff and management.

The Besley Commission, as the group became known, presented their report, 'On the Concept of Transition and Transition Impact: Implications for the EBRD', to the Board in June 2009. They started by noting that transition should be seen as part of a wider process in which economies develop a "balance between state and market", and where there are "multiple solutions to providing an effective market economy". Whereas traditional economics largely took for granted the institutions needed for a market economy to flourish, they said, a modern institutional approach looked at the appropriate roles for states and markets and, in particular, whether the state has appropriate incentives to deliver its proper role.

Two particular challenges for state involvement could be commonly identified in emerging economies: the competence of the state as an institution

15 Guriev was appointed as the EBRD's Chief Economist in 2015.

to allocate resources and the role of competing interests. In the Commission's view, good governance required a system that allowed the market to flourish while holding "powerful interests that try to influence the state in malign ways ... at bay", and the best way to achieve this was through building effective state institutions. This included a role for various groups to be able to hold the state to account, such as the media, unions, business associations and NGOs.

One example of this thinking concerned privatisation.

> Whether ownership should be private or public to achieve the best outcome is far from clear a priori ... setting up transparent, competent and efficient institutions to ensure that these industries are run in the public interest matters more than who owns the assets.

The report touched on the role of democracy, where they noted the link between effective markets and democracy was indirect and experience "heterogeneous". Nonetheless, the report pointed out there was a "strong correlation between prosperity and democracy" and to understand the relationship it was important to look at specific institutional structures and cultural norms.

In thinking about the activities of the EBRD in the context of a more modern approach to economics, the Besley team concluded that the Bank's original mandate was still valid since it was consistent with broader goals. In particular, they argued, social cohesion and broad-based increases in living standards were needed to deliver well-functioning and sustainable market economies. "Without these foundations, there is always a risk of reversal of past progress." Hence, they felt better recognition, especially in the assessment of operations, was needed for measures that reduced inequality of opportunity and promoted the legitimacy of market-supporting institutions.

The Besley Commission also highlighted sectors like health and education that had featured prominently as issues of concern to people in the *Life in Transition Survey*. They nonetheless realised this might be controversial and not within the immediate reach of an institution like the EBRD with its focus on the private sector.

The transition assessment process generally functioned well and they were impressed with how far the question of transition impact was "ingrained

in the corporate culture of the EBRD and provides coherence to its activities", a lasting impression on Guriev as he confirmed over a decade later.[16] Furthermore:

> The internal discipline of transition impact measurement and the EBRD's mission-driven corporate culture reinforce each other. This is an achievement that should not be underestimated. As the economic literature on mission-driven institutions suggests, the co-existence of non-profit mandates and for-profit incentives is very delicate. EBRD is an institution that has both; hence, it is quite remarkable that it has both been profitable and has been generally promoting its original mandate.

They did pick up on some of earlier controversies, however, noting that: "… the current framework seems less robust on how transition impact is to be assessed in more contentious areas like public utilities". On the issue of critical mass, they argued the notion that the systemic impact of further projects in the same sector suffered from diminishing returns should be revised. They suggested instead a more programmatic approach be considered, or at least one where irreversibility effects, such as demonstration effects, network gains and innovation, could be valued more effectively.[17]

The Besley Commission analysis also considered the Bank's transition indicators. The nine indicators of transition progress first compiled for the *Transition Report 1994* for each country of operations covered areas that were relevant at that time, including enterprise privatisation and restructuring, markets and trade, financial institutions and infrastructure reform. They were highly visible externally and used by other international institutions and academics.

The Besley Commission felt however that the indicators were not properly linked to the analysis of projects and the sector transition gaps that had emerged with the Bank's business expansion; nor did they fit country

16 Interview, February 2021.

17 In the past programmatic approaches had been frowned upon as they were associated with the World Bank's method of allocating large sums to governments to spend in areas like health and education which were largely outside the EBRD's agenda. The Chairman's Report on the AEB notes on Article 13, sub-paragraph (ii), "Delegates described the precise form of programme lending in which the Bank could become involved as 'projects, whether individual or in the context of specific investment programmes', so as to make clear that fast-disbursing policy-based lending is not included." See Kilpatrick, *After the Berlin Wall,* Chapter 1, p 35.

strategies. The lack of an aggregation process made it difficult to assess the overall impact of the EBRD.

On the other hand, looking at the story so far, the Commission felt reassured by the positive relationship between increases in EBRD lending and improvements in the indicator scores, and that EBRD lending scaled by GDP was greater in countries with poorer indicator scores. The group also felt that other indicators compiled by OCE, such as the Sustainable Energy Index and the *Business Environment and Enterprise Performance Survey* (BEEPS), as well as the *Life in Transition Survey* (LITS) could be better integrated with the transition assessment methodology. Similarly, they called for an additional series to measure the quality of state institutions along the lines of the World Bank/IFC's *Doing Business Survey*.

Wrapping up their assessment, the Besley Commission emphasised that while initially there had been a lot of optimism on reliance on markets, "reversals are possible" and that it was "crucial to focus on factors that create resilience and sustainability in markets". Emphasising the role of "market supporting institutions, including an effective state" they concluded: "Transition is about building 'well-functioning and sustainable markets'."

3. Incremental Methodological Improvements

The Besley Commission's report did not lead to wholesale immediate change—nor was it intended to do so—but it helped to progress a series of steps designed to improve the operational aspects of the transition methodology.

Integrated approach

One of the first actions following the Besley Commission's report was the introduction of what was called the Integrated Approach (IA). The idea was first explained in an information session for the Board in November 2009. Following the observation that the link between the project level and country level analysis was weak, OCE set out how this might be tackled. But rather than tying project objectives directly to country objectives the focus was on the next level up, by adopting sector reform packages, which fitted more comfortably with the project origination structure in Banking.

An IA was defined as a "coordinated sequence of investment projects, technical assistance, policy dialogue and cooperation with other stakeholders … that aim together to deliver measurable sector reforms …".[18] It gave room for portfolio solutions that went beyond the use of frameworks which to that point had been mainly based on collections of similar small projects, such as wastewater treatment projects in multiple municipalities. Instead, it prompted an ex ante assessment of a particular market and the transition challenges it faced and how a selection of projects and their cumulative impact (and thus critical mass effects) could improve its functioning, especially when combined with technical assistance, for training staff in new methods, and policy dialogue to change market regulations, for example.

Overall, it attempted to coordinate the economists' understanding of sectoral structural needs with bankers' projects and regional offices' knowledge of local conditions and make use of their contacts, particularly with relevant government ministers and officials. Care was taken to explain that an IA did not amount to programmatic lending nor was it a policy-based finance product. Each project within the IA had to have its own valid transition rationale but the presumption was that taken together the impact of the set of projects and associated work would be greater than the sum of the parts. It matched the Besley Commission's view that a critical mass of projects might support structural and institutional change more readily than a single project.

IAs started to appear in 2010, beginning with urban transport in Belgrade and then the Ukrainian power sector, and later involved sectors such as agribusiness, district heating, railways, private equity, venture capital, gas, renewables and some others.

Transition indicators

Following advice from the Besley Commission that the existing transition indicators no longer served the purpose for which they were originally constructed, a decision was taken in 2010 to switch to a set of sector indicators. These were based on a comprehensive assessment of transition challenges (ATCs) across the EBRD region and illustrated the scale of sector transition gaps facing each country. These were more relevant to the types of operations conducted by the Bank than the original indicators.

18 'An Integrated Approach to EBRD Operations', 13 November 2009.

Instead of broad themes such as large-scale privatisation or price liberalisation, the new indicators comprised 16 sector categories, five each for infrastructure and financial institutions and three each for industry and energy.[19] The degree of advancement in transition was again represented on a scale from 1 to 4+, with 1 representing little or no transition progress and 4+ indicating that "the standards of an industrialised market economy" had been met.

A variety of indicators from external sources and surveys relevant to individual sectors, including some of those employed previously, were used to build the composite picture. The choice of indicators allowed each sector gap to be divided into two categories: 'market structure' and 'market-supporting institutions and policies'.[20] The gaps were then measured against industrialised market economy yardsticks and assigned to categories from 'negligible' (advanced market level) to 'large' (little or no progress from a state-run economy).

The indicators provided a basis for setting priorities in country strategies and a starting point for project appraisal. The annual *Transition Report* also identified progress in transition using these sectoral indicators. Over time the number of sectors expanded and some areas were subject to detailed analysis to identify and monitor particular gaps, for example in SME requirements, sustainable resources, youth, gender and (within country) regional gaps.

Low-carbon transition

Attention to the environment, particularly when it came to activities in the public sector, remained a prominent concern.

Following the introduction of the Sustainable Energy Initiative (SEI),[21] the scaling up of the EBRD's green activities had begun in earnest. The

19 Infrastructure comprised roads, railways, urban transport, waste and wastewater, telecommunications; financial institutions covered banking, insurance and other financial services, capital markets, private equity, MSME finance; industry was made up of agribusiness, general industry, real estate; and energy was composed of electric power, natural resources and sustainable energy.

20 For example, the agribusiness sector's aggregate score was based on a 50:50 weighting of market structure and market-supporting institutions and policies, where the former was made up of the components development of private and competitive agribusiness (40%), development of related infrastructure (25%), development of skills (20%), and liberalisation of prices and trade (15%) and the latter legal framework for land ownership, exchanges and pledges (40%), enforcement of traceability of produce, quality control and hygiene standards (40%), and creation of rural financing systems (20%). 28 sub-indicators were used in all. See Table 1.1.1, 'Recovery and Reform', *Transition Report 2010*, p. 6.

21 The Sustainable Energy Initiative is described in Chapter 9, p. 349 et seq.

Besley Commission had encouraged the Bank to consider environmental sustainability as part of the system, and international interest in climate change solutions was growing more generally. For instance, the EBRD's former Chief Economist, Nick Stern, one of the key global influencers on the economics of climate change, was promoting at the LSE and in a new book his concerns about the slow pace of actions to tackle climate change.[22]

The EBRD's pursuit of climate goals through investments in public entities, such as electricity generating companies, continued to put pressure on the economists to accept carbon reduction as a transition activity. The Besley Commission had also emphasised the value of multiple projects in a particular area as a means of generating momentum for change. Climate-related activities fitted the bill admirably.

The existing system was under considerable stress.

In a nutshell, the problem was how to account for the value of non-market elements that lay outside the formal project, such as CO_2 reductions.

The Besley Commission gave impetus to those seeking changes to the transition impact system, so in September 2009 a further step was introduced.[23] Investments in, and subsidies for, sustainable energy were treated as compensating for inadequate price signals.

The scale of environmental outcomes was seen as relevant since the commitment by countries to carbon reduction targets indicated an urgency of action.[24] As such, large investments achieving significant CO_2 reductions or a critical mass of smaller investments doing likewise were factored into the analysis. Transition impact could be achieved in this context by fostering innovative solutions and supporting their diffusion to the critical point from which the private sector was able to take over and finance projects without EBRD support.

This interpretation relied on identifying a pre-existing 'best available technology' (BAT). Should the investment yield material carbon reductions (or reductions of other pollutants) in excess of a BAT baseline in a given sector and country, the demonstration of an improved use of technology was

---

22 Nicholas Stern, *A Blueprint for a Safer Planet: How to Manage Climate Change and Create a New Era of Progress and Prosperity* (London: Bodley Head, 2009).

23 'The Transition Impact of Projects Promoting Energy Efficiency and Lowering Carbon Emissions', 9 September 2009.

24 The UK introduced the first global legally binding climate change mitigation target set by a country with the passing of a Climate Change Act in 2008. https://www.lse.ac.uk/granthaminstitute/explainers/what-is-the-2008-climate-change-act/

counted as having transition impact. Where policy dialogue led to a similar result in reducing carbon emissions, for example through the development of carbon trading, this too was considered valid transition impact.

The modification of the system brought some relief. But pressures from the business side to expand climate change activities and from the policy perspective as the EBRD became more heavily engaged in the global climate change agenda meant that further adjustments were needed. These came with the next stage of thinking on the transition concept, and as advocates of a low carbon transition built a strong argument in favour of valuing carbon reduction outcomes as much as economic impacts. The Green Economy Transition (GET) programme (see Chapter 9) provided the methodological underpinning for a more general approach towards 'green' outcomes.

4. Modernising the EBRD

The new President launches a 'modernisation' drive

When Suma Chakrabarti arrived as President at the EBRD in the summer of 2012 the Bank was in good shape. Business volume was at an all-time high and there had been a return to profitability after the significant losses of 2008 and 2009.

Like many of his predecessors, he began with an internal stocktake. Chakrabarti had ideas for shaking up the organisation to what in his view would make it more effective and efficient through the introduction of modern management practices and with a focus on results. But he also had an eye for the EBRD on the world stage.

Two decades earlier Chakrabarti had attended the Bank's inauguration as private secretary to the UK's Development Minister and, as a former head of the UK Department for International Development (DfID), had a good understanding of the role of the EBRD in the wider development context.

He was aware that over the years a tension had grown between the original view of transition and current development thinking. Whether it should be called transition or not, he thought the issue was what the EBRD needed to do then to help its countries of operations transform their economies into more sustainable markets that were able to grow and compete in a globalised world.

He valued highly the role of reform and the part that policy dialogue played in achieving change in developing economies and wondered whether the EBRD was getting enough leverage from its substantial investments in countries of operations. The passage of time since 1989, the widening of the EBRD's shareholder base and a new region of operations also pointed to the value of some updated thinking on the Bank's conceptual underpinnings, especially if the EBRD was to feature more prominently in the development milieu and retain its relevance in a 'post-transition' world.

There were also structural management issues to sort out. The Besley Commission's advice and ideas had not resulted in a comprehensive solution to underlying methodological questions, nor had the subsequent changes fully resolved tensions between the economists and the Banking Department.

So, as Chakrabarti embarked on a radical shake-up of top management and the Bank's processes in search of effectiveness, he gave a green light to further thinking on the transition concept and the methodology that underpinned the Bank's investments, advice and strategies.

The starting point for change was a series of internal reviews of structures and processes. Chakrabarti was keen to set his own stamp on internal arrangements. The programme began with an efficiency drive and changes to the top management team structure.

A number of task forces were set up in the second half of 2012 to look at ways to improve efficiency and effectiveness. Some focused on the banking side, such as the Task Force on Sector and Product Innovation, while others considered issues surrounding the transition methodology (on results and IAs) and policy dialogue.[25] The most significant changes were seen in results reporting—an area in which the Bank was regarded as weak compared with its MDB counterparts. Efforts were also made to improve the incentives for bankers to take on more difficult projects, including through IAs. Work on policy dialogue only began to make real progress a few years later.

In keeping with the President's view on the need to improve the EBRD's strategic focus and policy capacity, a new senior management committee was set up, the Strategy and Policy Committee (SPCom).[26] Henceforth

25 The Task Forces reported in November 2012.

26 Its membership comprised the Vice President Policy and Partnerships as Chair, a Banking representative, one from CSE (later renamed Economics, Policy and Governance (EPG)), one from Corporate Strategy, one each from the Offices of the Secretary General and the General Counsel, with the Country Strategy and Results Management (CSRM) team acting as secretariat.

country strategies, donor funding issues, evaluations and other strategic and technical questions not considered appropriate for the Executive or Operations Committees would be fed through this committee.

The terms of reference of the previous Vice President for Operational Policies were revised[27] to create a new position of Vice President, Policy and Partnerships (called VP3), who acted as Chair of the committee. The role reflected Chakrabarti's view that the Bank needed to strengthen the visibility of its policy work and take a closer interest in its growing reliance on donor funding.

The changes had consequences for the role of the economists. OCE was split with the research group remaining under the Chief Economist while the other parts of the Department, covering projects and country work, were assigned to the new vice presidency under a new banner, Country and Sector Economics (CSE). In due course (in 2015), VP3 was merged with the Banking department to create the Client Services Group (CSG).

This finally brought about a change Chakrabarti had sought from the beginning, which was to integrate the majority of the economists more closely with bankers, including a shift of economists into the field. The hope was to lessen the long-standing conflicts between the two departments and improve understanding on both sides, as well as use the economists' sectoral reform expertise more effectively.

While OCE remained an independent voice under its Chief Economist, who reported to the President as before, transition assessment and the rating of projects fell to VP3. When VP3 was integrated into CSG, the reporting line of sector and country economists switched to the First Vice President, the most senior member of the Banking Department. This raised questions about conflicts of interest and the potential objectivity of the project appraisal process.

An innovative plan was then launched to streamline procedures and minimise this risk. The idea was to simplify the project assessment process and reduce the role of sector economists' judgement by providing bankers with a menu of questions to fill in for their projects.[28] The self-assessment system subsequently became integrated in a wider revamp of the Bank's project systems and processes under a broader efficiency drive (called Operational Effectiveness and Efficiency, or 'OE&E') and related IT enhancements.

27 In two iterations: first to Vice President, Policy and then to Vice President, Policy and Partnerships.
28 Project Christopher, as it was known, is described in more detail later in this chapter.

For the majority of projects, this provided adequate guidance on their suitability and tracking against results' targets. With complex cases, or those where issues arose as with the use of concessional finance or local content requirements for example, the views of OCE could be sought though need not be decisive. Ultimately, project decisions rested with the members of the Operations Committee.[29]

'Stuck in Transition' and its implications

While the task forces conducted their work, Jeromin Zettelmeyer, Berglof's new deputy, and his research team grappled with more fundamental developments.

Although most economies in the EBRD region had begun to recover from the immediate effects of the global and eurozone financial crises, growth in 2013 remained sluggish nearly everywhere. A projection in that year's *Transition Report* pointed towards a much lower long-term growth path than pre-crisis.

A comprehensive analysis picked out a number of reasons behind this conclusion and why many EBRD countries now appeared to be stuck in transition.

Initially, the large productivity gap between east and west had been reduced by market-based reforms. Price liberalisation, privatisation, foreign investment and an opening up of trade in the 1990s together provided a solid start to the convergence of transition countries with the more advanced west. Overall, productivity improved rapidly as the poorly used or idle resources of Soviet times were put to better use. As markets developed and expanded, incomes began to accelerate towards more advanced economy levels.[30]

However, many of these changes were one-offs as obsolete capital was eliminated and the production structure adjusted to the requirements of market economies. By the time the new century dawned, as the authors of the *Transition Report* noted, "the 'productivity catch-up' phase associated with opening up to the outside world and international integration has ended in most transition economies."

---

29 As part of the changes, the Chief Economist no longer remained a member of OpsCom.

30 In economists' jargon, improvements in total factor productivity drove the productivity increase more than growth in the labour force or capital stock.

By the mid-2000s, the good news was that productivity in EBRD countries of operations had reached comparable levels to those of other emerging economies with similar income levels. Further progress however depended on reform, especially to market-supporting institutions.

The Chief Economist explained the next steps that were needed to raise the quality of economic institutions:

> Beyond liberalisation, stabilisation, and privatisation, this encompasses regulation, effective government, strong rule of law, low corruption, and other aspects of the business environment … [and] … their ability to provide economic opportunities to individuals regardless of gender, region of birth or social background.[31]

But the reform process had been losing momentum. Berglof wrote that a "compelling concern is the stagnation in reforms and in improvements to market-supporting institutions in most countries in the region since the mid-2000s".

Unless reforms to economic and political institutions accelerated, the view was that the EBRD region would be destined to remain in a low growth orbit over the longer term with the result that "convergence with Western living standards … will not be achieved in most countries".

Behind this view was an analysis which showed a clear correlation between inadequate economic and political reforms and a lack of economic progress. An earlier assessment had shown that during the first decade of transition successful reforms were more likely to occur in countries with stronger political competition and less polarised electorates. The new analysis demonstrated a strong causal impact of democracy on the success of reform. Political turnover and strong executives helped to push back on elites who otherwise profited from state subsidies, insider privatisation and weak enforcement of the rule of law.

The *Transition Report* thus argued economic institutions could improve on the back of political reforms and that this was a reciprocal process:

> Just as stronger economic institutions support democracy so democratic change can influence the quality of economic institutions … Successful economic and political institution building reinforce each other.

31 *Transition Report 2013*, Foreword, p. 8.

But it also suggested the stifling of opportunities could lead to a dwindling of public support for reform:

> Market reforms that fail to benefit the population as a whole will not enjoy public support for long. … As in the case of Egypt, a lack of inclusion might help to explain why populations turn against market-oriented reform …

Berglof summarised the overall picture in a frank but sobering conclusion: "The recent history of transition has shown that weak political institutions and entrenched interest groups can cause countries to become 'stuck' in transition."

Chakrabarti quickly latched onto the implications for the Bank. The *Transition Report* vindicated the rationale behind the EBRD's economic and political mandate. As the Besley Commission had suggested, transition was first and foremost a political economy process. It was not a simple task of applying propositions found in standard economics textbooks.

Tangible improvements from market engagement were needed. A new catchphrase, "We invest in changing lives", appeared alongside the Bank's logo to reflect this view, added by Jonathan Charles, the Managing Director of EBRD's Communications. Structural reforms, difficult though they were for investment bankers to manage, began to be regarded as important to the Bank's work as raising the stock and quality of capital through its investments.

What the analysis brought home clearly was the importance of good governance and inclusion in designing a successful transition strategy, as well as the traditional need to develop competitive and integrated markets. Chakrabarti understood that the EBRD had to strengthen these aspects of its work in a way that aligned with its investment banking objectives. The Report provided the intellectual underpinning for this, and for the internal reorganisation which promoted the policy dimension and brought the economists' understanding of structural reforms together with the investing and execution skills of the bankers.

The hoped-for result would be a stronger role for policy work alongside investment efforts. And, if it could be managed, to be able to use the EBRD's investment and advisory capacity as leverage for reform—political and economic—to advance the transition process, even if that meant pulling back when reforms were heading in the wrong direction.

Work remained to be done, however, especially on the transition concept and how any update might be translated into the deeply embedded operational assessment system.

Inclusion

A little ahead of publication of the 2013 *Transition Report* a paper to the Board reported on work to modernise the transition impact methodology.[32] This was the culmination of discussions that had been taking place since the Results Task Force had reported the previous year. There were two important developments: one on how to relate inclusion to transition while the other dealt with the project scoring and incentive system.

The Besley Commission had set the ball rolling on thinking about the role of social outcomes in transition and was followed in 2012 with the publication of an influential book in development economics by Daron Acemoğlu and James Robinson.[33] The authors argued that inclusive economic institutions supported prosperity by raising productivity and generating incentives that encouraged investment and innovation, whereas systems that mainly benefitted a well-connected elite failed to successfully deliver long-run growth. But it was the impact of the Arab Spring and the arrival of new countries of operations with glaring deficiencies in gender equality and large-scale youth unemployment that accelerated the Bank's work on inclusion.

The paper explained how inclusion issues could be integrated into the transition methodology, not as a matter of political economy, although this was relevant, but as a matter primarily of market efficiency. The focus was on economic rather than social inclusion. Defining inclusion in relation to equality of economic opportunity and selecting three prominent areas of (ex ante) inequality to address—gender, youth and regional disparities—the issue fitted neatly into the existing framework, albeit with a new look in some areas. The key channels for responding to demands for more inclusive market economies covered market expansion (via access to labour markets and market-based finance), skills enhancement, higher business standards and corporate governance and through demonstration effects.

---

32 'Modernising the Transition Impact Methodology', 17 June 2013.

33 Daron Acemoğlu and James Robinson, *Why Nations Fail: The Origins of Power, Prosperity, and Poverty* (New York: The Crown Publishing Group), 2012.

An important innovation, in keeping with the transition impact methodology, was to build specific transition gaps by country for each of the three components.[34] Once done, a pilot study was run to gauge the feasibility of applying the assessment of inclusion to projects. This was necessary as there were some uncertainties whether bankers would find a role for inclusion in their projects which were normally justified on grounds such as increased competition or a new production process.

It turned out—in some cases to the bankers' surprise—that about one-third of the sample of almost 90 projects in the pilot showed potential impacts from inclusion. What was especially encouraging was that many clients showed a willingness to tackle inclusion issues, helping to reassure bankers there was mileage in the idea from a business perspective. The southern and eastern Mediterranean (SEMED) region showed the largest potential.

Some Board Directors were nonetheless wary of any extension of the existing methodology, fearing it could prove a distraction from delivering on the core of the Bank's mandate. There were arguments too over whether inclusion should be treated outside the existing transition assessment system rather than inside it. But a wider group agreed with management's view on its incorporation within the existing methodology and there was genuine enthusiasm among many Directors to see progress in opening the Bank up to these new areas, especially on gender equality and improving the skills of young people where the challenges in the SEMED region, and in Turkey on gender issues, were clearly very large.[35]

Expected transition impact (ETI)

The second strand to the "modernising transition" paper was more technical. In accounting for its results to the Board, emphasis was laid on transition impact as well as business volume and profitability. Its basis was the project-level scoring system carried out by the economists whose results were aggregated into an overall Bank performance indicator. Bankers' scorecards and performance rewards were related to this measure at the sectoral level.[36]

---

34 See the *Transition Report 2013*, Chapter 5 'Economic Inclusion in Transition'.

35 For more on inclusion, see Chapter 7.

36 A further gripe among bankers was the fact that there was no similar scorecard, or hard-edged constraint, for economists.

For some time there had been concerns among Board members that the system did not incentivise bankers to go the extra mile in search of more difficult projects. Many bankers did in fact try hard to find bankable deals in difficult territories and to encourage clients to take on extra risks with their support. But this was not always the case and there was an element of truth to the Board's concern.

Another weakness of the system was its limited treatment of risk to the delivery of transition results. Projects were rewarded on their potential but the risks involved in whether promises or aspirations made were actually met were simply noted. It meant, for example, all kinds of reform promises might be agreed between a banker and, say, a state-owned client to cut a deal which would offer enough potential impact to pass the transition test but realistically might have negligible chances of being delivered.

The proposal made was that the expected transition impact of projects should be the basis of assessment. In other words, the combination of a project's potential impact and the probability of its delivery in full. This was a more logical approach, and one which mirrored the appraisal of financial risk.[37] To make it work, a system of numerical scores (rather than labels such as "Good") was introduced, based on a statistical analysis, which balanced the two components. There was enough evidence from the previous system of scoring to assess probabilities of success at different levels of potential impact and assign these probabilities to the new system.

A further advantage of the new approach was to be able to tilt the scores in a progressive way to reward bankers' efforts to pursue the most difficult or risky (from a transition perspective) projects. A previous top-scoring project ("Excellent") was now, at 100, worth almost twice as much as its previous next level down ("Good") at 60. This mattered to the average score on which the Bank[38] and bankers' rewards were judged[39]: previously an "Excellent" project had been valued the same as a "Good" project.[40] Similar incentives were

37 The notions of probability of default (PD) and loss given default (LGD) mapped into transition impact potential (impact given delivery) and risk to delivery (probability of success).

38 The target for ETI set at Bank level was a minimum annual annual average score of 60 across all new rated projects. There was an analogous system for the portfolio, Portfolio Transition Impact (PTI), which also had an annual target. See 'EBRD Scorecard: Proposed Expected Transition Impact (ETI) Matrix', 6 November 2013, p. 12 and Kilpatrick, *After the Berlin Wall*, Chapter 10, section 5.

39 Rewards were based on several additional indicators of success, especially business volume, profitability and disbursement of funds. Nonetheless, the EBRD placed a high weight on transition parameters.

40 The previous scorecard target was based on reaching "at least 80 per cent Good or Excellent projects". See 'EBRD Scorecard', p. 4.

offered for projects seeking to tackle difficult delivery risks, as often seen in less advanced countries. An ETI Matrix set out the parameters accordingly.[41]

The Board welcomed the ETI approach and it was introduced for all projects from 2014 onwards.

Country strategies

For many years country strategies had played only a limited role in the formulation of policy and strategic direction at the EBRD. For the most part, they resembled a wish list of projects bankers hoped to sign over the coming period.

An effort was made to improve the situation in late 2010, when management declared they intended to produce "streamlined and more focused strategies" with "clearer prioritisation", and in 2013 there was a further push. But neither added up to a major change of outlook. A year later a country strategy results framework (CSRF) was introduced.

It was the arrival in 2015 of Philippe Le Houérou, a former World Bank Regional Vice President, that started a more radical overhaul of country strategy work. The timing coincided neatly with a rethink on the transition concept that was launched around the same time (see below) allowing a closer integration of project and country level activities.

Looking at the existing procedures and their deficiencies, Le Houérou, who took over as the new Vice President for Policy and Partnerships, referred to medical practices. "If you plan to treat a patient," he would say, "you must first make a thorough diagnosis". Yet, the strategies on which the EBRD planned its investments and advice offered no such diagnostic work.

Although Le Houérou left the EBRD in early 2016, after being appointed as Chief Executive Officer of the IFC, country strategies thereafter were built on the three pillars he had advocated: sound diagnostics, targeted interventions where the EBRD could make a difference, and good coordination with other international actors active in the country.

A new group in VP3, Country Economics and Policy (CEP), led by its director, Artur Radziwill, a former Polish Deputy Finance Minister, set about preparing diagnostic studies focused on barriers and opportunities facing the private sector in a number of countries. More sensitive political dimensions were left to the country strategy documents themselves. The

41 'EBRD Scorecard', p. 10.

analyses were designed to provide an understanding of the economic situation and structural factors in each country and a rationale for the intended interventions by the Bank in its country strategies.

The first diagnostic report covered Egypt and was presented to the Board in September 2016[42] as a first step towards the EBRD's inaugural strategy for the country. An in-depth diagnostic for Kazakhstan[43], a country the Bank knew well, followed in November and thereafter diagnostic analyses came with the regular flow of country strategies. One feature of the Kazakh study, and used in later studies, was work by the sector economists which drew on developments initiated by the transition concept review, in particular, an assessment of transition qualities by country.

Policy dialogue

As part of the effort to improve country strategies and delivery of transition results Le Houérou was keen to raise the EBRD's capacity to conduct policy dialogue with country authorities. Supporting reform-minded governments effectively was an important goal which President Chakrabarti also strongly supported.

Le Houérou's World Bank knowledge, where policy discussions formed a major part of country assistance, was one motivating factor. Those operations were mostly sovereign loans, whereas the great majority of EBRD lending was to the private sector. At the IFC, the World Bank's private sector lending arm, policy efforts were left primarily to the World Bank's global practice expertise. There was no such constraint at the EBRD.

Unlike the IFC, the EBRD provided a moderate amount of sovereign lending and so would engage with governments. It also was heavily involved in dealing with state-owned entities and public-private partnerships (PPPs), and with the municipal sector. The EBRD's presence on the ground with active local offices in every country gave it visibility and access; and as a major international investor it was a key interlocutor with convening power in many of the smaller countries it served. There was significant potential for policy engagement (a term Le Houérou preferred

42 'Private Sector Diagnostic: Egypt', 2 September 2016.

43 'Kazakhstan Diagnostic Paper: Assessing progress and challenges in developing a sustainable market economy', 4 November 2016.

to policy dialogue) with the authorities, particularly when matched with investments and expert technical help.

The Strategic and Capital Framework (SCF) for 2016–2020, *Re-energising Transition*, agreed by Governors in May 2015, made the objective clear: "The Bank will have a significant, structured policy dialogue capacity, leveraging its project work and aimed at sector reform and institutional and governance improvements."

A paper was presented to the Board in September 2015. At its core was a focus on supporting policy reforms. The view was that policy priorities should be decided up front as part of the country strategy, based on the diagnostic analysis and concentrating on areas where the EBRD held comparative advantages. A stronger role for policy advice and reform advocacy was introduced, including 'communities of practice' to strengthen knowledge management and share the work programmes of different teams engaged in reforms and policy dialogue. A better linkage between demand-driven investments and policy reforms to improve the business environment and raise standards was envisaged. Here it helped that bankers and economists were working closely together in the field and at London headquarters, as part of CSG, with VP3 and Banking jointly responsible for delivery of results.

Le Houérou's temporary successor before the arrival later in 2016 of Pierre Heilbronn, a top French civil servant, was Alain Pilloux, a very experienced EBRD insider. Pilloux pushed hard to embed the improvements quickly and fully, especially within Banking. He was in a good position to do so with over 20 years of banking experience, including running country offices. His efforts, together with those of Mattia Romani, the VP3 Managing Director of Economics, Policy and Governance (EPG), led to the introduction of priority policy objectives as part of bankers' and economists' annual objectives. These formed a qualitative measure of every participant's performance, which were reviewed region by region by the Vice Presidents of Banking and VP3 each year.

5. A Revised Transition Concept

Berglof, the longest serving Chief Economist at the EBRD, left the Bank at the end of 2014 to head the Institute of Global Affairs at the LSE.[44] Follow-

44 Berglof was appointed as Chief Economist at the Asian Infrastructure Investment Bank (AIIB) in 2020.

ing his departure, Lankes who was Managing Director, Corporate Strategy, acted as Chief Economist before Guriev arrived to take up the role in September a year later.

Chakrabarti now turned his attention towards the transition concept. The issue for him was whether to keep it.

His development background—where he was strongly associated with DfID's goal of reducing poverty—chimed with a wider questioning of the concept of transition. There was a matter too of how the concept might fit with his vision for a coordinated skills-based MDB architecture, an idea he had recently espoused in a lecture at the Petersen Institute alongside Donald P. Kaberuka, President of the African Development Bank.[45] Was the notion of transition still relevant or "somewhat passé" as the Besley Commission had themselves asked?

The SDG agenda

There were important additional reasons for pushing forward with a review of the transition concept in 2015. This was the year the 2030 Agenda for Sustainable Development—and the Sustainable Development Goals (SDGs)—was due to be agreed (by 193 countries) at the UN General Assembly in September. It was to be preceded by the Third UN International Conference on Financing for Development in Addis Ababa in July.[46] It was evidently going to be a highly significant year for development.

The agenda was particularly relevant to the EBRD because most IFIs and their government shareholders had come round to the view that the private sector was critical to the delivery of the now expanded set of global development goals. Plans were in train for the Heads of MDBs to promote the idea of 'billions to trillions'—the notion that public sector institutions could work together with the private sector and leverage huge sums of finance for development—at the Spring Meetings of the IMF and World Bank in April.

With the promotion of private sector finance lined up to be a major plank of the forward development agenda, this was a major opportunity to show how the EBRD had the tools and knowledge to meet these

45 Among the ideas was the suggestion of joint ventures, something that had been discussed separately with the African Development Bank. Suma Chakrabarti, 'The New Multilateralism: The Role of Regional Development Banks', lecture at the Petersen Institute for International Economics, 8 October 2014.

46 The previous conference was held in Doha, Qatar in 2008.

ambitions. Chakrabarti did not want the EBRD to be left on the sidelines as a result of being seen to follow an outmoded concept at such an important moment.

Taking stock

Lankes, who knew the history of the transition concept better than anybody else in the Bank and had helped steer much of the earlier work by the Besley Commission, took up the challenge almost immediately on his appointment as acting Chief Economist. He launched an internal review to consider the relevance of the concept for modern market-oriented economies and its operational status.

At an information session with the Board to launch the Transition Concept Review in February 2015 he argued that the post-war focus on a distinction between public and private goods, where the latter were viewed as best left to markets, reached a peak with market liberalism in the early 1990s, just as the EBRD was establishing itself. However, since then the emphasis of economists had shifted towards new dimensions that needed to be taken into account. In particular,

- The role of market-enabling institutions, particularly in the context of important externalities such as climate change;
- Recognition of the complexities of sound market regulation and its enforcement;
- The role of incentives, social capital, trust and corruption;
- An increased focus on inclusion; and
- A more nuanced view of the state in industrial policy, including support for SMEs.

In the early phase of transition, privatisation had been used to strengthen incentives and governance but when it occurred in a poor institutional context it resulted in unfair outcomes and poorly-run firms. Poor quality competition policies and state capture by private interests elsewhere also imposed costs on growth.

The experience of many EBRD countries of operations, especially outside central Europe and the Baltics, had shown corruption to be serious. It was worse among resource-rich countries. The Besley Commission's earlier

advocacy of a free media, free elections and an independent judiciary to reduce the extent of corruption had been hard to put into practice in many countries.

The focus on institutions, with reference to world-wide experience, pointed towards a view that while transition had a clear direction there was no unique end-point. Differences in history, culture, economic structures and individual preferences meant that routes taken and solutions found need not match precisely. But, as could be seen in differences between institutions in European countries and the USA, successful democratic market economies could emerge despite these differences.

Building on the Besley Commission assessment and the 2013 *Transition Report*, Lankes reminded the audience that a lack of social cohesion and inclusion undermines the legitimacy of market systems. It was the absence of democratic and market freedoms that had ultimately led to the demise of central planning and inequality of opportunity threatened a similar fate in other systems, as had been seen in the Arab uprisings of 2010-11. Inclusion needed to be taken into account since it could help build constituencies for market reforms and democracy, as well as adding to economic efficiency and avoiding blocks on market liberalisation resulting from excessive wealth accumulation in the hands of the few.

In addition, modern economies increasingly relied on information and knowledge, which were public goods. Knowledge creation, such as in research and development (R&D), involved risky projects. Their social returns are generally higher than private ones since other players can benefit from new knowledge. As such, public-private solutions were often needed with, for example, the state providing some risk capital for start-ups alongside private finance to leverage successful innovation for subsequent market deployment and viability.

The description of how Lankes and his team saw the building blocks of the modern-day economy, and the contrasts with the thinking of 20 years earlier, was well-received by the Board who, like management, hankered after an updated view of transition ideas. The next step would be the preparation of a paper with a set of methodological proposals.

Besley II

The Besley Commission six years earlier had provided valuable methodological insights that helped the Bank adjust some of its methods. However,

these changes were made mainly within the limits of the system that had been introduced in 1997. With the EBRD's 25th anniversary due in 2016, Chakrabarti and Lankes hoped that the revamp envisaged under the concept review might lead to a new approach to transition.

As part of the preparations for the review, Lankes contacted Besley that autumn to see if he would lead a group of experts again, this time focusing on improving the qualities of market economies and the outcomes they generated. Lankes asked Besley for a framework that "should be simple and understandable for a broader audience, and lend itself to being operationalised."

Besley once more assembled a panel of experts. Guriev, now at Sciences Po in Paris and known to be coming to the EBRD as its next Chief Economist, remained on the panel but Dewatripont was replaced by Beata Javorcik, a Professor of Economics at the University of Oxford.[47] Their report was submitted in March 2016.[48]

The intervening years had reinforced the message of the Besley Commission of 2009: "Specifically, it suggested a greater focus on the importance of stability, governance, a concern for gender equality among other dimensions of inclusion, competitiveness, and innovation … and a more intensive appraisal of the appropriate role of the state …"

The experience of financial crises, rising inequality of income and wealth within countries and a change in the Bank's geographic focus towards countries with young, growing populations facing serious problems of inequality of opportunity pointed to important new dimensions that the EBRD needed to explore under its transition mandate.

The terms of the debate concerning transition had changed since the euphoria of the fall of the Berlin Wall and its immediate aftermath. The then 'model' market democracies, such as the USA and UK or Sweden, had demonstrated they contained major fault lines. In truth, they offered no ultimate assurance of stability or guarantee of progress. The once lauded idea of an 'end of history' was a mirage. The move from plan to market was just one step; the road from market towards a high-income economy was vastly more complex.

47 Javorcik became the EBRD's Chief Economist in 2019.

48 T. Besley, B. Javorcik and S. Guriev, 'Transition Impact and the EBRD's Mandate', Review Panel Report, March 2016.

Becoming stuck in a middle-income trap[49] was not unique to the EBRD region. Countries needed to find their own policy routes to become successful market economies. Furthermore, failure to include disadvantaged and disenfranchised groups in the political economy process along the way was likely to hold back progress in transition or, worse, put it into reverse.

Beyond the EBRD region the world and its policy preoccupations had changed too. The Cold War stand-off between east and west had been replaced by a new existential threat: the perils of climate change for the planet and with it the quality of human life. The EBRD had been quick to recognise this and act on it. But more needed to be done. Furthermore, greater attention in the development context was being given to the issue of gender equality, a matter which the EBRD had also begun to address.

The panel felt the EBRD had a strong ability to apply its investments and advice to both causes while continuing to help many of its countries of operations escape the middle income trap. But to be effective in doing so the Besley team believed that the Bank needed to reorient itself and give more prominence to the actions it was able to take to deliver on these global public goals. They said:

> The EBRD's capacity to contribute to the wider debates about economic development and its determinants is less clear, … the EBRD needs to develop a distinctive voice … the transition impact framework needs refreshing in line with wider goals, many of which have become *de facto* areas of interest for EBRD.

Although the group called for a "fresh interpretation" of the transition concept and its application they saw no case for changing Article 1 of the AEB. This "gives a distinctive mandate for EBRD and makes it unique among IFIs", they said. But, they added, "a market economy is no guarantee of success in and of itself" and requires "a complementary role of an effective state". Here, they argued, legal capacity (the ability to enforce contracts and regulate fairly), collective capacity (insurance to cover the inadequacies of market provision), and fiscal capacity (non-distortionary revenue raising) were essential for a well-functioning market economy.

---

49 The tendency for emerging economies to make only slow progress after reaching certain levels of per capita income.

They recommended that the organising principle for the EBRD should not be transition as it had been understood in the past but as:

> Supporting a move towards a competitive, well-governed, sustainable and inclusive market economy. This means paying attention to building state capacities as well as investing in private capital.

The Besley panel's conclusions were important since they brought together areas which the Bank had begun to pursue in a somewhat disjointed way without clearly articulated links to its mandate. The proposed refreshed interpretation of transition provided a coherence that had been missing. A well-functioning market economy was thus not simply one that followed competitive and integrated markets, but one that was also well-governed, being supported by an effective state, inclusive and environmentally sustainable.

A number of other recommendations were made by the panel, notably concerning country strategies which they believed should be given a more central role and be more closely linked to the Bank's operational strategy and project-based lending.

Qualities of a sustainable market economy

The Besley team, supported by Nik Milushev and Alex Plekhanov in OCE and Lankes, interacted intensively with the Board during the months in which they prepared their analysis. First at a workshop in November 2015 and next at a Board retreat held at the LSE in February 2016 for which several Directors, who had been encouraged to offer feedback and ideas, issued "gray" papers[50] of their own on how they saw the transition concept 25 years on and matters concerning its implementation. Lankes later described the process of Board involvement as "the most significant in [his] 30 years of working in IFIs!"

The panel's paper was well-received when it was discussed at a further Board workshop in March. At the final workshop on 21 April the Director for the Netherlands, Paul Vlaanderen, acting as a coordinator of Directors'

50 'Grays' is a term used at the IMF for written statements by Directors ahead of meetings. It derives from the colour of the paper on which such papers are printed.

informal inputs, including his own, summarised their thinking on the topic. Although there were differences in emphasis it was essentially in line with the approach suggested by the Besley panel and the Lankes team. There was almost universal agreement that the transition concept needed refreshing and that the paper provided a sound basis on which to do so.

Based on those discussions, two more qualities of sustainable market economies were added to the list: resilient and integrated. Emphasis on resilience reflected the scars of the global financial crisis. Integrated highlighted the importance of countries' internal and external connectivity, such as the integration of capital markets, infrastructure, trade and knowledge.

Following the panel's report and a further period of collecting views from Directors and others in the Bank a paper, *Transition Concept Review*, was prepared and presented to the Board on 2 November 2016. Taking its cue from the Besley panel, it set out a fresh interpretation of the transition concept.

There were two key propositions which the Board was invited to endorse. First, there was a clarification that the Bank's mandate was to foster *sustainable* market economies. This was argued to be fully consistent with Article 1 of the AEB. Second, that such an economy may be characterised by six primary qualities so that "a sustainable market economy is competitive, well-governed, green [environmentally sustainable], inclusive, resilient and integrated". This implied a focus on outcomes, and on market-based decision-making that leads to those outcomes, rather than stopping at market structures per se. The authors of the paper regarded this as its core conclusion.

The six transition qualities also formed the basis of project and country level assessments of transition, on the one hand by asking bankers to explain the main transition qualities their projects were targeting and on the other hand by dissecting country diagnostics and strategies according to the transition gaps shown for each quality.

A great advantage of the "qualities" proposal was its simplicity—something the bankers welcomed with great relief—and that outcomes at last appeared to matter to the Bank. They always had done but they were no longer obscured by a focus on the structural characteristics of markets. What was left unsaid in the propositions the Board endorsed, but was made clear in the paper, was that the EBRD remained a bank which pursued systemic change and the transformation of markets to make them more sustainable.

The Bank is to foster a change in economic systems, i.e., in the way that economic decisions are made, rather than directly pursuing development outcomes. This choice was based on the conviction that a well-functioning market economy and private initiative—set within a political framework of democracy and pluralism—are most effective at delivering on people's aspirations. The Bank's mandate is therefore unique only in degrees: it targets the means rather than the ends, but it cannot lose sight of these ends.

No-one disagreed with that.

The Six Qualities of a Sustainable Market Economy

Competitive

A competitive market economy has:

- Market structures with enough players to ensure competition among firms, and rules making it easy to enter and exit;
- The capacity for firms to generate added value by producing more efficiently or innovating; and
- Incentives to compete and advance, based on private ownership and management, and, with public entities, governance that ensures commercially sound decision-making.

Well-governed

Governance concerns authority, decision-making and accountability in all domains. At its core, governance is about the quality of institutions and the processes that they support.

A well-governed market economy rests on two pillars:

- National or subnational economic governance, that is the institutions and processes that support economic activity and economic transactions by establishing the rule of law, transparency, accountability, checks and balances and fair play;
- At the corporate level, the system of rules, practices and processes by which companies are directed and controlled in accordance with international standards.

Green

A green or environmentally sustainable market economy is one in which economic decisions reflect the full value of resources to present and future generations.

Operationally, it is where economic decisions seek to limit the impact on the environment, achieve ambitious outcomes—such as carbon emissions reductions—and where market failures are addressed through policy and legal frameworks.

Inclusive

An inclusive market economy ensures that anyone—regardless of their gender, place of birth, socio-economic environment, age or other circumstances—can access labour markets, finance and, more generally, economic opportunity.

Promoting an inclusive market-based system is about efficient (human) resource allocation rather than social policy. But there is also a political dimension to inclusion. Democratic institutions make access to power more open, directly supporting inclusion and the political and social sustainability of market economies.

Resilient

A resilient market economy supports growth while avoiding excessive volatility and lasting economic reversals. It is about the ability of markets and market-supporting institutions to resist shocks, about policy predictability and about balance and sustainability in financial and economic structures.

Resilience objectives are most commonly associated with the nature, conduct and structure of financial systems. Financial stability refers to a financial system's ability to withstand shocks without major disruption in financial intermediation and in the supply of financial services. At best, it also suggests the absence of excess volatility, stress or crises.

Integrated

Integration refers to connectivity with the global economy through trade and investment and other cross-border dimensions and to the (geographic) integration of domestic markets.

An integrated market economy has the policies, institutions and connectivity—through energy, infrastructure and information technology links—to minimise the transaction costs of trade, support competition in product and services markets, and tap a wide range of financing channels.

Integration is a central element in any economy's competitiveness. It enables trade at greater speed, lower cost and better quality. It is critical to growth and job creation.

6. Operationalising the Changes

In order to operationalise the revised concept a system built around the six transition qualities was needed. The qualities worked well for banking teams[51] so the framework could remain principally sector-based as before and would pay attention to the country context. An additional advantage of the qualities approach was that it could be linked more easily to the SDGs than the previous system.

Project Christopher [52]

As the transition concept review got underway a parallel exercise was conducted to improve the transparency and predictability of the impact

51 There were some obvious matches where qualities like resilient would be frequently cited in transition impacts by financial institutions' teams, green with energy efficiency and climate change work, competitive in industry, commerce and agribusiness projects, and so on. Nonetheless, these were not exclusive: green and inclusive worked across all sectors for instance.

52 The project was named after the code-breaking effort using one of the earliest computers, the Enigma machine, designed and called Christopher by Alan Turing, which was used to crack Nazi Germany's coded messages during World War II. It was the subject of a film, *The Imitation Game*, released at the end of 2014, starring Benedict Cumberbatch in the lead role.

assessment system. The sector economists engaged in what was essentially a decoding and distilling of past project assessments by sector to extract the core questions that needed to be answered to pass a test of transition impact adequacy; and from there the degree of impact that was associated with different levels of ambition. A greater impact could be expected, for example, to result from the training of SME suppliers of a large retailer with the view to expand supply networks and upgrade the quality of SME products, or from dedicated policy work to structure public service obligations of municipal water companies.

Under Romani's guidance, and interactions with the banking teams, a semi-automated system based on sets of questions relevant to particular sectors was built up over time, piloted and integrated into work designed to simplify the full set of processes followed by the Bank in its operations (Project Monarch[53]).

The core of Project Christopher identified the primary transition quality being addressed by the project, along with a secondary quality (which received less weight), and generated a preliminary score to reflect the strength of its potential impact. This was then adjusted for the context in which the investment was being made: first for the degree of challenge it faced (the "transition quality gap"), and then for the extent to which it targeted a country priority, with the very best such projects receiving a bonus score ("star projects"). Additional adjustments were introduced for equity and local currency to reflect their particular value and difficulty and to provide an additional incentive for bankers.

Transition quality gaps: the ATQs

The ATCs which had provided an overview of the transition challenges by sector were replaced by a similar system based on transition qualities, the assessment of transition qualities (ATQs). These were first published in full in November 2017,[54] although had begun to be used internally as part of Project Christopher before this, and like the ATCs were designed to test the degree of advancement in the transition of EBRD countries of operations.

53 Project Monarch was the name given to the successor to OE&E when the Bank's operational processes were brought together under one systems-wide data management IT project.

54 See 'Structural Reform', *Transition Report 2017–2018*, 'Sustaining Growth', pp. 105–115, 13 November 2017.

For the purposes of country diagnostics and country strategies the analysis of qualities showed where a country was most lagging behind—in terms of, say, its competitiveness or inclusion credentials. Projects in areas with larger gaps were given a rating uplift.[55]

Mapping the system to the SDGs

Unlike the Millennium Development Goals, which focused on reducing poverty and other social outcomes like health and education, the SDGs were broader and emphasised issues such as the environment, employment, infrastructure, and inequality which were more relevant to the activities of the EBRD. At the same time, the notion of transition qualities encompassing the green economy and inclusion matched the SDGs far better than the previous system.

Figure 6.2 The Six Transition Qualities and the SDGs

55 'Transition Impact Methodology Update', 6 July 2018.

Of the 17 SDGs, the revised EBRD transition impact assessment system was associated with 13 of them, from gender equality and decent jobs to sustainable cities and climate action, as illustrated in Figure 6.2. This helped with the presentation of country strategies to audiences outside of the Bank, since it was easy to see where and how the EBRD was tackling various SDGs.

Conclusion

The outcome of the transition concept review was an almost universally accepted success. Although contrary views were heard at the Board when it was agreed in November 2016—on the basis that it diverted the Bank from the original concept and its mandate—the vast majority was in favour of its adoption.

Lankes, who was about to leave to join Le Houérou at the IFC as Vice President for Economics and Private Sector Development, was widely praised at the meeting for leading the thorough review and for his many contributions to the Bank's development since his arrival at the EBRD in its early days. Directors applauded especially the open way in which their views had been sought during the course of the review.

Within the Bank too the new system settled in well. Bankers in particular were pleased with the results. One senior banker said enthusiastically "At last I can explain transition to my clients and what our investments relate to!" It was a far cry from their refrain a decade earlier.

For Chakrabarti it was a vindication of his perseverance to modernise the EBRD. The Bank was better placed among its peers than before and more visible in its tackling of problems facing emerging markets and developing countries in the third decade of the 21st century.

Rather than banishing the concept that underpinned the Bank's philosophical stance Chakrabarti embraced the new interpretation as a relevant metric for developing economies and the future. Efforts could now be focused on transforming markets towards sustainability through each of the six quality dimensions.

The initial EBRD goals of competitive and integrated markets had been connected to qualities of resilience, inclusiveness, good governance and "greenness" through a better understanding of developments in economics and the role of the state, practical experience and lessons from the crises of the past decade. Financial meltdown had pointed to the need for resilience.

Inequality of opportunity and corruption, notable in the Arab Spring and Ukraine, showed inclusion and good governance were key to ensuring the legitimacy and irreversibility of democratic and market orientations. The climate crisis indicated how human progress would be undermined without market-based solutions supported by public interventions and incentives.

Building towards the sustainability of market economies was the way forward.

Chapter 7
Equality of Opportunity

Introduction

On 8 November 2016, the EBRD launched its annual *Transition Report*: 'Transition for all: Equal opportunities in an unequal world'. It was a response to the negative side of globalisation. Globalisation lifted many hundreds of millions of people out of poverty but left others stranded on the margins of growing global prosperity.

The good news for the Bank's region was that countries were becoming richer. Remarkable successes had been achieved in the post-communist societies that the EBRD had been created to support. The region had finally closed the "happiness gap" with people on similar incomes in other regions. The residents of former communist countries were "now expressing just as much satisfaction with life as their peers in other countries".

But that positive revelation belied a negative underlying trend. Not everyone had profited equally from the rising global prosperity. There had been some very obvious losers as well as winners.

One of the panelists discussing the *Transition Report* during its launch event was Serbian-American economist Branko Milanović, who had famously illustrated the distribution of globalisation gains with a graphic shaped like an elephant.[1]

1 The "elephant chart", as it became known, first appeared in Christoph Lanker and Branko Milanovic, '*Global Income Distribution: From the Fall of the Berlin Wall to the Great Recession*', World Bank Policy Research Working Paper 6719, December 2013, https://openknowledge.worldbank.org/handle/10986/16935.

The tip of the elephant's rising trunk showed how globalisation had disproportionately favoured one very tiny proportion of the global population—the super-rich.

The graphic description of the disparate global distribution of incomes was consistent with an increasing concentration of wealth, which the EBRD said was pronounced in the EBRD regions.

"In particular, the transition process appears, in a number of countries, to have contributed to a strong concentration of wealth among the very rich," the *Transition Report* noted.

The report showed how an uneven distribution of gains had also left its mark on post-communist transition economies. People in these countries were suffering from both real and perceived levels of inequality.

In EBRD regions, "people are overwhelmingly of the view that inequality levels are high and rising. These perceptions may, to a significant extent, be guided by the fact that wealth is strongly concentrated among the very rich," the report said.

The feeling of being left behind by those experiencing decades without improvements in real incomes is often cited as one of the principal causes behind a rise in populism during this period.

In his foreword to the report, the newly-appointed EBRD Chief Economist, Sergei Guriev, wrote: "If mainstream politicians want to withstand the challenge presented by opportunistic populists, they need to design reforms that do more than just deliver growth on average in the long run. Reformers need to ensure that they enjoy the support of the majority at all times." [2]

He added, "reforms should deliver benefits to the majority of the population in both the short and the long term, preventing populism both in times of crisis and in normal times."[3]

Coincidentally, the EBRD's report had been launched on the very day of the US election that took Donald Trump to the White House, an event that would become emblematic of the growing backlash against globalisation.

The rising concern about inequality would put the whole concept of inclusion more firmly on the agenda of the EBRD. At the 2017 Annual Meeting in Cyprus, the Bank launched its first Economic Inclusion Strategy. By the end of 2020, inclusion was one of the three dominant objectives

2 *Transition Report 2016–17*, Foreword, p. 8.
3 *Transition Report 2016–17*, Foreword, p. 8.

for the EBRD's strategy for the next five-year period, alongside support for a green, low-carbon economy and the acceleration of digital transition.

Inclusion was now mainstreamed in the EBRD. However, the Bank had taken a long and winding road to this destination.

1. A Missing Gender Agenda

In its very early days, the EBRD had placed a high priority on developing the market economies in its region and helping them become more competitive and more integrated within the global market place.

There was little or no focus on issues like inclusion, or gender equality. Like climate change, they might be important concepts—but they were not considered the remit of the EBRD.

Egalitarian paradise

There was another reason why gender had less resonance. The EBRD was dealing with countries that had emerged from a system which on paper guaranteed the equal rights of men and women.

As political scientists Ellen Carnaghan and Donna Bahry wrote of the Soviet Union in a 1990 essay: "official doctrine has declared gender differences to be socially irrelevant".[4]

There were indeed many more opportunities for women in the Soviet Union. While only four women ever served in the Politburo, women not only participated in but also played significant roles in the workplace.

Alexei Stakhanov, the Donets Basin miner, may have given his name to the concept of the overachieving Soviet employee—the hardworking Stakhanovite. But there were plenty of female Stakhanovites, especially working on the land—like the tractor driver Pasha Angelina and the beet producer Maria Demchenko, both Soviet heroines.

There were clear female role models, such as the cosmonaut Valentina Tereshkova, the first woman to fly in space. Tereshkova was an engineer at a time when this was not an obvious profession for women in the USA or

4 Ellen Carnaghan and Donna Bahry, 'Political Attitudes and the Gender Gap in the USSR', *Comparative Politics* 22, no. 4 (1990): 379–399.

western Europe. In contrast to counterparts in the west, women in communist countries could and did excel in the STEM disciplines of science, technology, engineering and mathematics.

There had been in the Soviet Union "a sharp rise in the rates of women's participation in the labour force—higher levels combined with deeper penetration into occupations previously considered 'male'", according to a 1985 paper published in the *Journal of Labor Economics* (JOLE).[5]

But, for all the celebration of Soviet technological and industrial heroines, the real story was very different from the Soviet doctrinal version.

As the JOLE article continued, there were indeed inequalities between men and women. "Considering the proportion of working mothers of small children even the number of day-care centres for young children is inadequate." While many women may have had good day jobs, the task of looking after the household fell squarely on the shoulders of women. Other outcomes, according to the paper, included low salaries relative to those of their male colleagues.

If the position of women was tough in the Soviet Union and other communist countries, it became even more so once the regimes had crumbled and economies collapsed. But it was still several years before the gender issue would be taken seriously by the EBRD.

Building advisory support

In line with its mandate to promote environmentally sound and sustainable development, the EBRD had published an Environmental Policy in the very first year of its existence. "Environmental" in the document had a wider sense than the purely ecological, covering social issues such as the protection of workers' rights and those of vulnerable members of society. However, even when the Board approved a second update to the Policy on 29 April 2003, there was no reference to gender or any nod to the role of women.

On 8 March 2003, when the EBRD with other MDBs and the IMF voiced support for gender equality on International Women's Day, their joint statement[6] argued that gender equality accelerated economic growth.

5 Gur Ofer and Aaron Vinokur, 'Work and Family Roles of Soviet Women: Historical Trends and Cross-Section Analysis'. *Journal of Labor Economics* 3, no. 1 (1985): S328–S354.

6 Statement from MDB/IMF Heads on International Women's Day, 8 March 2003.

Otherwise, it touched on goals that were not part of the EBRD's day-to-day vocabulary—reducing poverty, hunger and child mortality, creating educational opportunities, promoting maternal health and combating diseases like HIV/AIDS and malaria.

There was one area where EBRD activities specifically targeted women around this time. An adjunct to the Banking Department, the largely grant-funded TAM/BAS teams had been created in 1993 with the aim of helping to develop the micro, small- and medium-sized enterprise sectors.

The TurnAround Management (TAM) and Business Advisory Services (BAS) programmes promoted economic transition through advice and mentoring at the enterprise level. The TAM/BAS group saw the potential for women to strengthen skills levels in the enterprise sector and determined that encouraging participation in business would help TAM/BAS to achieve its goal of promoting transition to market economies.

2004 saw the launch by BAS of a small-scale Women in Business Initiative in Azerbaijan, running a workshop for women, in cooperation with the Soros Foundation. A larger initiative began in November 2005, with funding from the Canadian International Development Agency (CIDA). The objective was to support women entrepreneurs who wanted to start up their own businesses, and also to help the growth of established women-owned enterprises.

Within a year, the BAS offices in the south Caucasus, in Armenia, Azerbaijan and Georgia, had delivered 15 focus groups and workshops for women in business and 30 BAS projects with women in micro, small and medium-sized enterprises.

But TAM/BAS was an advisory programme and not fully integrated with the main business of the EBRD. As a result, these BAS programmes for women were kept quite separate from the activities of the wider Bank.

Gradually however, the concept of gender would move up the EBRD agenda. Around this time, the EBRD carried out a Gender Equality Study to assess gender issues in countries of operations that showed how gender inequalities in the EBRD region had increased during the transition period.

The study[7] concluded that the change in the role of the state had entailed negative consequences for women by reducing their economic opportunities, access to social services and ability to affect political decisions.

---

7 The study is referenced in the TAM/BAS Strategic Plan 2008–2010, September 2007. https://www.ebrd.com/downloads/tambas/country/briefs/Tambas_plan.pdf.

This underutilisation of human capital was a constraint on economic development and hindered the achievement of the full benefits of transition to a market economy.

In 2008, a gender element was introduced in the updating of the Environmental Policy, which was expanded to become the Environmental and Social Policy (ESP). The social element in the broader policy covered such areas as labour standards and working conditions, as well as community impacts, including public health, safety and security—and gender equality.

One further development in 2008 was the EBRD's formal endorsement of the third of the Millennium Development Goals (MDGs), which aimed to promote gender equality and empower women.

On 7 March 2008, the Danish government had launched its MDG3 Champion Torch campaign, a specific call to action on the gender-focused MDG. The idea of the initiative was that MDG3 Torches would be carried by 100 Torchbearers—representatives of governments, the private sector, civil society, the media and international organisations.

EBRD President Thomas Mirow was one of these 100 world leaders who accepted the MDG3 Gender Equality Torch from the Danish government and pledged to pursue the MDG3 objective.

For his part, Mirow committed to launching and implementing a Gender Action Plan (GAP) in the Bank's countries of operations. The EBRD would actively promote greater opportunities for women and aim to counter the effects of gender inequalities in the region. The job now was to come up with just such a plan.

2. Gender Action Plan

Over the next year, a small Gender team was set up in the Financial Institutions (FI) team in the Banking Department. It was led by Chikako Kuno, the Director of the Small Business Finance team, and contained a gender specialist.

In July 2009, the team took the first draft of a Gender Action Plan concept to an Information Session for the Board of Directors.

The Gender Action Plan (GAP) paper conceded that the Bank had not "consciously promoted gender equality prior to 2008". Nonetheless, despite the absence of any specific initiatives to promote gender equality, the

EBRD's work over the previous 17 years had "undoubtedly resulted in positive long-term benefits for women".[8]

Its support for transition, economic growth and sustainable projects had helped to improve the overall quality of life and standards of infrastructure. These developments had had a clear positive impact on women as well.

But now it was time to do more:

> The arguments grounding the Bank's present gender initiative are compelling. They justify the resources and efforts that will be invested to ensure that—more than merely paying lip service to gender—the Bank contributes to concrete advancements with relation to gender equality and women's empowerment through its investment and technical cooperation projects. The Bank is now seeking to develop a structured approach to gender equality to mainstream it throughout its activities and measure progress in relation to gender equality and the empowerment of women.

The arguments were backed up by evidence confirming the negative impact of the transition process on women. Female labour force participation had dropped between 1990 and 2005 in the majority of the transition countries. Where women had returned to paid work they were tending to take low income jobs where professional education was not required.

Governments were spending far less on public care schemes and the job of looking after either the young or the old shifted from the public sector to private individuals, which in practice meant women. Many women were forced to choose between formal employment and acting as carers.

An analysis of the types of jobs available in 2000 showed that the majority of men were active in permanent and self-employed positions, while the majority of women were in "subsistence jobs", unpaid workers within the family or on the land, or they had no form of employment at all.

Women remained at a disadvantage in some transition countries as far as access to finance was concerned. Firms managed by women were less likely to obtain a bank loan than similar firms managed by men. There were indications that female-managed firms were charged higher interest rates—a trend more prominent in countries where transition was least advanced.

---

8 The EBRD's Gender Action Plan, a concept paper presented at a Board Information Session on 13 July 2009.

The GAP envisaged a series of steps starting with mainstreaming gender across the Bank's entire investment and technical cooperation activities. This included making sure project appraisal processes took account of gender. It would make operational the reference to gender in the new ESP, and make sure gender equality was seen as an indicator of good corporate governance in projects.

The EBRD would also raise gender awareness internally within the Bank though information campaigns and internal events. It would carry out pilot projects to map out and assess the impact of the EBRD's investments and develop tools to measure and monitor this impact. It would leverage its position on the supervisory boards of companies to raise gender awareness and also seek to collaborate with other IFIs/NGOs to implement the plan.

Under the GAP, three pilot countries, Georgia, Kyrgyz Republic and Romania, were chosen where projects would be developed in order to strengthen gender equality and women's empowerment.

Around this time, Biljana Radonjic Ker-Lindsay headed the NGO relations team based in the EBRD's Communications Department. It would fall to her to finalise and implement the GAP.

Radonjic Ker-Lindsay recalls being approached by Horst Reichenbach, then Vice President for Risk Management, Human Resources and Nuclear Safety. Reichenbach asked her to lead the gender plan implementation and make sure that gender could fit in closely with the EBRD's broader objectives.

"In addition to the public pledge by President Mirow and the support of very senior management, the pressure to act was coming primarily from certain Board members. There had also been appeals to the Bank from civil society, which was part of the reason why I had been chosen to work on the issue," Radonjic Ker-Lindsay said.

She realised that there was not much appetite at this stage within the Bank to take gender work a lot further, with no real activity beyond the Women in Business (WiB) advisory services, which were semi-detached from the EBRD's central activities.

One of her first responsibilities was just to raise awareness of the gender issue and increase buy-in within the Bank, to discuss what gender challenges lay in the EBRD's countries of operations and what the EBRD could do about them within its transition mandate.

"It was important to make clear how drastically the position of women had deteriorated since the collapse of communism and the disappearance of the sort of social support that had previously been available," she said.

The team worked on the plan through the rest of 2009. Radonjic Ker-Lindsay identified three specific areas that remain key targets for support for women over a decade later. "Women in the workplace" looked at employment opportunities for women and working conditions. "Women in the market-place" looked at the role of women as entrepreneurs. "Women in the community" looked specifically at how women accessed basic services and how local infrastructure served their requirements.

Until that time, the Gender team was only going to the Board to inform Directors about ideas developing around the gender issue.

A 26 October Information Session, however, decided that the Board of Directors should formally approve the Gender Action Plan, demonstrating a higher level of commitment to its principles. That endorsement came on 29 January 2010.

Nine months later, the EBRD Board approved the Bank's first gender pilot project under the GAP, a municipal investment in Romania. The Bank's investment to modernise streets and street lighting in the Transylvanian city of Sfantu Gheorghe took account specifically of the needs of women. The project looked at women's travel patterns, noting that in general they made more trips than men, because they travelled both for work and for domestic tasks such as shopping. Eighty per cent of women walked to work, compared with 60 per cent of men. The proportion of women on lower incomes who walked to work was much higher, because buses were too expensive or inconvenient. Women were particularly worried about the poor lighting in residential areas and did not feel safe walking in the streets during the evenings.

The second pilot in 2010 focused on a waste management project in Adjara in Georgia. It specifically targeted women in campaigns about waste reduction, recycling and community cleanliness, primarily on the basis that it was women who would share the information with their children. The project also aimed to ensure equal opportunities for men and women working for the company operating the landfill.

A third pilot put a focus on women's requirements in a project to upgrade the water infrastructure in the Kyrgyz capital of Bishkek. Women were much more involved in the use of water than men—for cooking and

washing. Women were also more concerned with the quality of water, while men tended to value permanent water supply over quality.

When the Gender team delivered an update on its activities to the Board in October 2011, a whole new dimension had been added to the gender initiative following the Arab Spring and the EBRD's tentative first steps in a new region.

Gender issues in a new region

While the EBRD had already made a successful start in its activities outside of the former communist countries of central and eastern Europe with its expansion into Turkey in 2008, the addition of four and possibly several more countries with a completely different social heritage added a new layer to the EBRD's gender work.

It was important in the context of the GAP to assess what specific characteristics the gender question might have in the southern and eastern Mediterranean countries.

An analysis presented to the Board showed that considerable progress had been made in improving maternal health and reducing infant and child mortality in the region. However, progress was slow in areas like women's ownership and control over assets, and their ability to inherit.

Young Arab women were doubly disadvantaged in the labour force, for being young and for being women. Youth unemployment rates were already problematically high. In 2010 in Jordan, for example, 48 per cent of women aged 15–24 were unemployed, double the rate of 24 per cent for young men, according to International Labour Organization (ILO) data.

The GAP paper referred generally to scope for the EBRD in the creation of micro, small and medium-sized enterprises (MSMEs) in the southern and eastern Mediterranean and said economic growth in the region would depend to a large extent on the creation of the MSMEs with a specific focus on promoting female-owned businesses.

Women were seen as a large untapped resource in these countries. There were, however, considerable challenges, including the presence of a large informal economy where most MSMEs operated outside the formal sector.

Women were disproportionally represented in the informal sector and in segments of the informal labour force with the lowest earnings, including home workers.

3. Time for a Gender Strategy

Having laid solid foundations for EBRD activities in the gender sphere, Radonjic Ker-Lindsay moved from her position as GAP coordinator in May 2012, handing over to Michaela Bergman, the Chief Counsellor for Social Issues, based in the Environment and Sustainability Department.

Bergman was a senior social expert, with responsibility for gender issues within her team and a fervent proponent of gender equality. Six months later, Bergman would go to the Board stating it was time to turn the Bank's gender activity up another notch. A presentation to the Board on 22 November 2012, proclaimed: "Gender – Time for a Strategy."

This was shortly after Chakrabarti had taken over as EBRD President, bringing to the job a very strong personal focus on equality of opportunity, both within the EBRD itself as well as in the countries where it invested.

Bergman circulated a draft strategy to the Board ahead of a Financial and Operations Policies Committee (FOPC) meeting on 28 February 2013. The paper outlined the rationale for the new Gender Strategy:

> Equality of economic opportunity should be seen as an intrinsic characteristic of a well-functioning market economy and therefore an intrinsic aim of transition. The development of a Gender Strategy therefore builds on the proposition that promoting equality of opportunity for women contributes to the main purpose of the Bank, promoting transition.

Over the three years of implementation of the GAP, progress had been made in mainstreaming gender into the Bank's operations. Now the time had come, the paper said, "to make gender considerations integral to the Bank's operations".

There was, however, only a brief discussion of the proposed new strategy at the 28 February meeting, as the following week Directors were due to hear from OCE about new proposals on the wider role of inclusion in transition (see Chapter 6).

On 7 March, Erik Berglof went to Board Directors to present the paper, flanked by a small team including Barbara Rambousek, an Austrian development expert who had joined the EBRD a year earlier to help develop a focus on economic inclusion.

There were by now two parallel strands in motion. The development of the Gender Strategy and the introduction of a more systematic approach to the whole concept of economic inclusion that the economics team had be working on since 2011.[9]

Berglof, and his deputy Jeromin Zettelmeyer, were actively promoting the concept of inclusion within the transition process. Berglof had brought Rambousek to the EBRD with the specific aim of helping to define (and subsequently to operationalise) inclusion.

While most Directors agreed on the importance of inclusion to the promotion of successful economies, not all of them were convinced it was necessarily an integral part of transition.

At the same time, a small but quite vocal group of influential Directors did not believe the approach to gender should be in the form of a Strategy, which - in their view - raised it to a too significant level of importance and official commitment.

As one Bank official closely involved with the discussions at the time recalled several years later: "This did point to the more serious problem that the Bank had struggled to take the gender issue seriously. To a certain extent, members of the Board had either been blind to the issue or been concerned that the EBRD might be losing its mandate and just degenerating into a [standard] development bank".[10]

Despite its name, a distinction had always been made between the EBRD, the transition bank, and other traditional development institutions.

The Strategic Gender Initiative

In order to allay those concerns, when the Gender Strategy was ready to go back to the Board, it was no longer a Strategy but a Strategic Gender Initiative (SGI). Complete with a recommendation from Chakrabarti, it was formally approved on 16 April 2013.

The SGI listed progress that the EBRD had made via the Gender Action Plan under the rubric of the three A's—"Access to Services", "Access to Employment" and "Access to Finance".

9 See also Chapter 6.
10 Interview, 2021.

Further municipal projects that took account of gender differences had been carried out, including a district heating investment in the western Ukrainian city of Ivano-Frankivsk where the EBRD financed capital expenditure aimed at reducing energy losses and improving the quality of heating and hot-water supplies.

As part of the investment, the utility company agreed to include a gender element in its corporate business plan and customer communication strategy.

One result of the initiative was that the utility made a greater effort to communicate with women because they were mainly responsible for paying the bills and more prone than men to raise complaints about poor levels of service.

Under "Access to Employment", one of five projects aiming for the promotion of equal opportunities was with Romanian oil group Petrom whose CEO and Chair Mariana Gheorghe became a symbol throughout the EBRD regions of the role women could play in industry.

Gheorghe had previously worked at the EBRD where, having joined from the Finance Ministry in Bucharest, she became a senior banker. After the privatisation of Petrom in 2004, she represented the EBRD on the group's Administration Council, and in 2006 Gheorghe became Petrom's General Executive Director. In 2013, Gheorghe ranked 27 in the Fortune List of the 50 most powerful women in business. She was the only manager from south-eastern Europe to have appeared on the list.[11]

It was at Petrom that the EBRD delivered its first gender pilot project focused on equal opportunities and best human resources practices. EBRD gender consultants worked with Petrom, a firm in an industry typically dominated by men, to identify where they could improve opportunities in the workplace for both men and women, focusing on recruitment, mentoring and career management.

In the "Access to Finance" section, the SGI highlighted the BAS outreach to MSMEs where the focus on gender had strengthened over the preceding years through tailor-made programmes aimed specifically at women in business.

---

11 The only other manager included from the EBRD's post-Communist region was Olga Pleshakova, the head of the private Russian airline Transaero Airlines, in 46th place. Ranked second on the list was the only other woman from the whole EBRD region, Güler Sabanci, chair of the family-controlled Turkish conglomerate Sabanci Holding.

From the first steps to provide support for women entrepreneurs in the south Caucasus, BAS reached out next to Ukraine, where discrimination against women in employment was common. And then to Moldova and Bosnia and Herzegovina.

However, by the time of the SGI, support for female-led firms had started to move out of the purely BAS realm and into the mainstream EBRD. There had been investments with Turkish banks which had specific envelopes for on-lending to female-led enterprises.

Oksana Pak was a senior banker in the Financial Institutions team in London at this time. She recalls starting work as early as 2009 on the first such Turkish credit line, to Garanti Bankası (GB). This was at the very beginning of the EBRD's activity in Turkey. "This was a 'plain vanilla' credit line which included a sentence stipulating that special attention would be paid to women-led entrepreneurs," Pak said.

Indeed, there was just a very brief mention in the 45-page document outlining the €50 million syndicated loan to Garanti Bankası, where the thrust of the loan's purpose was on lending to MSMEs outside of Turkey's three largest cities, Istanbul, Izmir and Ankara.

The brief rider read: "The Bank will provide medium term financing to GB as a bank willing to expand its franchise in the regions and for specific sectors and purposes (e.g. small agriculture and women entrepreneurship)." It was in 2012, Pak said, that the EBRD provided a loan to Garanti where the proceeds were targeted exclusively towards women.

This project went to the Board in September 2012 and the EBRD went public with the news in November. "This credit line … is the first in the history of the EBRD to be entirely dedicated to women-owned and operated SMEs," said Francis Malige, at that time Director for Financial Institutions in the southern and eastern Mediterranean, Turkey and Ukraine. [12]

The SGI said the project with Garanti aimed to increase the share of women-owned or managed SMEs in Garanti's loan portfolio, implementing a targeted marketing and communication strategy, providing managerial and financial literacy support and further increasing awareness and motivation throughout Garanti's management and branches.

12 EBRD Press release, 9 November 2012. 'EBRD gives funding boost to Turkish businesswomen'.

Also in November 2012, the EBRD announced a €50 million investment in Turkey's Yapi Kredi Bank. Of this total, €30 million was aimed at supporting SMEs in the agribusiness sector. The remaining €20 million would allow Yapi to finance SMEs managed and owned by women.

"Turkey can do much more to enable women to act as economic agents of transition," said Mike Davey, then EBRD Country Director for Turkey. "Women represent a huge resource that can help achieve Turkey's full economic potential."[13]

Other similar credit lines followed in Turkey in 2013, including a €25 million facility to IsBank and €30 million to Seker Bank.

4. Inclusion and Transition

In 2013, the economists continued to work on the integration of economic inclusion—and in this context also gender—into the transition process. The research was led by Zettelmeyer, together with Rambousek and economist Michelle Brock.

From late 2011 onwards, Berglof had put a particular emphasis on the topic, focusing on surprises that had been thrown up by the 2010 *Life in Transition Survey*, which had raised questions about the impact of the EBRD's work on equality of opportunity. Rambousek explains:

> There had been a belief before this that the transition process would lead intrinsically to economic opportunities for people across our region. But this wasn't the case. What we saw were huge discrepancies and these gaps were not closing. Because of this there was less and less support for reform and for democracy.[14]

It was clear that something had to be done. Rambousek was asked to develop the overall approach, both at the conceptual as well as operational level and started by reviewing existing work by others on equality of opportunity.

---

13 EBRD Press release, 20 November 2012. 'EBRD subscribes to asset-guaranteed bond programme by Turkey's Yapi Kredi Bank'.

14 Interview, 2021.

> We tried to see what that could mean for the EBRD. What the intellectual basis would be for integrating a focus on people into the context of a market level transition. We started to develop a methodology to understand inequality across our region, looking at characteristics such as gender, youth, place of birth and socioeconomic environment that shape access to economic opportunity but lie outside of a person's direct control.

This work formed the basis for of a chapter entitled "Economic Inclusion in Transition", which Rambousek co-authored with Brock, in the *Transition Report 2013*.

The research also laid the foundation for the introduction of economic inclusion in the EBRD's transition approach, which was to be presented to Board Directors in a series of discussions in the first half of 2013.

As part of this work, sector economists linked up with Rambousek to run a pilot project with Banking in late 2012 and early 2013 across eight countries of operations, looking at how inclusion might be incorporated in projects and how the transition assessment might be affected.

In the first of a series of meeting with Directors, on 7 March 2013, Berglof presented economic and political arguments for directly including inclusion in the methodology for measuring transition impact.

Economically, exclusion was inefficient. It undermined incentives to participate in economic activity. Politically, non-inclusive and grossly unequal systems were less likely to muster political support for market reform. This would increase the risk of reform fatigue and reversal.

Aware of the sensitivities surrounding the issue, Berglof said his team was not presenting a revolution but rather an evolution of the transition impact methodology. Economic inclusion is "already implicit in much of what we do, but we want to make it explicit".

"Some Directors were very sceptical or even completely against this," Rambousek recalled.

> One Director said: "The road to hell is paved with good intentions." Others said this was outside of our transition mandate and, if we took this path, we risked losing our triple-A credit rating. Many were worried about the EBRD branching out into something they thought was World Bank

territory. There was still very little appreciation of the distinct private sector focus that the EBRD could bring to this agenda.

There were some tense meetings but ultimately, in the wake of persuasive argument and tenacious negotiation, in particular by Berglof, a positive recommendation was made to the full Board which formally approved the new approach on 9 July 2013.

Rambousek said: "This meant that inclusion became a source of transition impact. We established how to do it, how to measure it and how to assign impact." After running the pilot, it was now possible to apply the transition assessment to actual projects.

In the initial phase, says Rambousek, it was still not clear how seriously the concept of inclusion would be taken. She remembers one senior economist in the team telling her: "If you want to stay in the EBRD you need to find a second string to your bow. This inclusion thing is not going to turn into a full-time job." Another senior EBRD manager said: "Gender people come and go. Find something else to do."

By 2021, as Director for Gender and Economic Inclusion, Rambousek was running a team of 35 people.

The final paper that went to the full Board was entitled 'Fostering Economic Inclusion within the Transition Impact Methodology' and explained OCE's proposals for going beyond the EBRD's existing transition impact approach.

While the EBRD already implicitly promoted inclusion, it would in future define transition gaps with respect to the capacity of economic systems to create economic opportunity for women, youth, and residents of less developed regions.

Projects that were expected to narrow an inclusion-related transition gap would receive credit in the same way as projects that were expected to narrow a particular sector gap.

Previously, investments in women-led firms had been treated in exactly the same way as loans to any other company. Now they would receive a higher transition value. That higher transition impact assessment would make such deals more attractive to the banking teams.

This was just one of the factors that supported the launch of the EBRD's fully-integrated Women in Business programme.

5. The Women in Business Programme

On the last Friday before Christmas in 2013, Valeria Della Rosa, a Senior Manager in the EBRD's Small Business Support (SBS) team, was sitting on the floor of her office surrounded by hundreds of papers and many documents that needed signing that evening by a managing director.

It was a race against time. If the contract that Della Rosa was preparing was going to go ahead, it had to be finalised by the end of the year. This was the last working day of 2013.

The only Managing Director available was Olivier Descamps and he was leaving for a skiing trip. Descamps agreed to stay around until each of the individual papers forming the contract was signed.

The papers related to a donor agreement between the EBRD and the Turkish Ministry of Labour and Social Security, for the use of funds made available to Turkey by the EU. This grant funding, worth a combined total of €38 million of EU money and a national contribution from Ankara, formed an essential—indeed the essential—element in the EBRD's first fully-fledged Women in Business programme.

Up to then, Della Rosa recalls, the EBRD had been struggling to take Women in Business to the next level, where advice and support and training for women entrepreneurs could be combined with significant levels of financing.

The next step would go beyond the few Turkish credit lines that had targeted women entrepreneurs and the BAS advisory programmes.

"We started to look at working with SIDA.[15] The Swedes were keenly interested in the issue of developing women entrepreneurs and eager to do something strategic with us," said Della Rosa.[16]

However, the next change came as a result of a fortunate constellation of related events, centring specifically around Turkey. The EBRD had built up very strong relationships with the key private Turkish banks in the relatively short time that it had been investing in the country.

The SBS team also had an extremely strong relationship with the EU as an important provider of grant funding. At that time, the EU had an unused supply of funding of some €30 million for Turkey, its Instrument for

15 SIDA, the Swedish International Development Cooperation Agency.
16 Interview, 2021.

Pre-Accession Assistance (IPA). And one clear objective of the EU at this time was that such funding be used to promote the increased participation of women in the workplace in Turkey.

The time pressure on that Friday evening before Christmas was that a deadline of the end of 2013 had been set for the utilisation of the IPA funds by the Turkish government. If they were not committed by then they would be returned to Brussels.

Rightly or wrongly (wrongly, Della Rosa would argue), the banks were seeking at this time additional reassurances before they would scale up their lending to women entrepreneurs. Providing credits to women was seen as risky. If the banks were going to join with the EBRD in any large-scale programme of lending to women, they wanted guarantees.

Della Rosa saw the EU funding as the perfect opportunity to provide the guarantees the banks wanted in order to proceed. She says:

> I was able to convince Francis Malige that with €30 million in guarantees we could build up a portfolio of €300 million in lending to Turkey. This was an important business opportunity. Francis agreed and became a major sponsor of the programme.
>
> It was a perfect combination. We had the great relationship with the Turkish banks. We had the great relationship with the EU, which had the funds we needed, and we had a sponsor in the Banking team. And we had proven tools to work with women entrepreneurs directly too with the SBS team.

The programme would be launched later in 2014 after Della Rosa and colleagues took a comprehensive plan to the Board including the proposals for what became a €338 million Women in Business programme for Turkey. The guarantees that were sought and delivered by the EBRD and financed by the EU funding were in the form called Risk Loss Cover (RLC), a risk sharing mechanism that aimed to reduce the perceived risk of lending to women entrepreneurs.

"As it turned out", says Della Rosa, "only a minute proportion of the €30 million risk funding ever had to be used. The fact is: women don't default. They are better entrepreneurs." The banks had believed the women's business sector to be more risky. "It wasn't."

With the guarantees in hand, Della Rosa and colleagues were in a position to develop a full-scale plan for a Women in Business programme. In

May 2014, a joint approach was taken to the Board from three teams, Support for Small Business, Financial Institutions and Gender.

The EBRD had been providing dedicated advice, under the BAS programmes, since the middle of the previous decade, and specialised credit lines, like the ones to the Turkish banks since 2012, so it had built up profound knowledge of gender in finance.

Against this background, the EBRD now had a "unique ability to bring together funding and advice into an integrated, comprehensive solution".[17]

The new proposals argued that, on the demand side, women-led SMEs had limited know-how and awareness of financial products and services which reduced their access to finance from formal channels. Women-led SMEs were concentrated in the services' sectors and often lacked adequate collateral. Social and legal restrictions around inheritance and land ownership rights tended to make this situation worse.

On the supply side, banks generally perceived women-led SMEs as a high-risk sub-segment, mostly operating on a microscale in the informal sector. Financial products were not tailored to the needs of women-led SMEs and there was little effort by financial institutions to understand this sub-segment and design tailored financial products or processes.

"There is a need for a comprehensive response to support women entrepreneurship which addresses, in an integrated manner, obstacles that women-led SMEs face to grow," the plan said. The RLC was a key element that would allow the EBRD to scale up the scope of lending to women. "The RLC will encourage PFIs (partner financial institutions) to lend to viable enterprises that might not otherwise have met standard lending criteria," the Women in Business plan said.

The RLC would allow for more relaxed collateral requirements, as well for the provision of longer tenors and investment finance with favourable conditions to women-led SMEs. The banks would also benefit from technical assistance to help them better understand women-led SMEs and tailor their products accordingly.

The plan now was to develop the programme for Turkey and then extend similar programmes to the Western Balkans and Croatia and the Eastern Partnership countries.

17 'Women in Business (WiB)—Comprehensive Programmes', Board Information Session, 22 May 2014.

Donor financing had been secured for Turkey in late 2013. At the 2014 Annual Meeting in Warsaw, an agreement was sealed with SIDA and the Luxembourg authorities for the programme in the Western Balkans. A donor agreement was later signed with SIDA for the Eastern Partnership scheme, with co-financing from the EBRD's Early Transition Country Fund, and the EU Neighbourhood Investment Facility (EU-NIF) supported the risk sharing.

The plan presented to the Board on 22 May was to deliver the three programmes between 2014 and 2017. Their total value, to begin with, was nearly €430 million. A total of €54.5 million was requested from donors, comprising €17 million for advice for PFIs and €37.5 million for risk sharing. The EBRD credit lines would total €375 million.

The EBRD launched its first Women in Business programme, in Turkey, in October 2014. The Bank put up €300 million, initially liaising with six Turkish banks: Finansbank, Garantibank, İşbank, Şekerbank, Türk Ekonomi Bankası (TEB) and VakıfBank.

After the introduction of the initial schemes, the programmes expanded into different areas, to Egypt in 2015 and then other SEMED countries and also into Central Asia.

By the end of 2020, Women in Business programmes were underway in 23 economies across the EBRD regions. Total financing had topped €500 million and, via over 50 different financial institutions, the EBRD had reached out to more than 90,000 women entrepreneurs.

Charlotte Ruhe was Director in the SME Finance and Development Group at the time of the Women in Business launch in 2014. Speaking in 2021, as Managing Director for Central and South Eastern Europe, and after a career at the EBRD spanning more than two and half decades, Ruhe said: "Women in Business was the programme that gave me the most personal satisfaction."[18]

In the early days, there had been a lot of work to refine the programme and make it more attractive to Bank partners. "Women have a lot of barriers to overcome in all the countries where we have offered the programme, and it was critical to make the link between access to finance and business advice."

Taking the programme into the southern and eastern Mediterranean countries meant the EBRD had been able to make an even greater impact.

18 Interview, 2021.

It was crucial to help motivate women in this region to grow their businesses. As Ruhe saw it,

> The impact of the boost of confidence, not to mention access to finance and knowhow to go with it, transformed countless women-led businesses. This is something about which we can all be proud! The challenge now is to 'push the needle' for women leading mid-sized businesses to grow them into large firms. I'm looking forward to this next stage in the journey.

6. A Strategy for the Promotion of Gender Equality

In December 2015, Bergman returned to Board Directors with proposals for what would now become a fully-fledged gender strategy, a Strategy for the Promotion of Gender Equality.

It was at the 2015 Annual Meeting that Governors had called specifically for the creation of a gender strategy as part of the Strategic and Capital Framework (SCF) 2016-2020. In its efforts to create more resilient economies, the SCF said the EBRD would:

> Further mainstream economic inclusion across its operations through measures aimed at improving the participation of marginalised groups in the market economy, and adopt a Gender Strategy to deepen the impact of the Bank's gender activities.

Accordingly, the Gender Equality Strategy responded by explaining:

> It aims to increase women's economic empowerment and equality of opportunities in the countries where the EBRD invests, as an important contributor to well-functioning market economies and inclusive societies—a core component of sustainable and equitable transition. The Strategy articulates the Bank's view that gender equality is a principal element in the promotion of sound business management and critical to the advancement of transition.[19]

19 Strategy for the Promotion of Gender Equality 2016–2020.

The paper pointed out that gender inequalities continued to constrain equality of opportunities, both globally and in the EBRD's countries of operations. Furthermore, women were significantly more likely than men to be unemployed, particularly when younger, to face difficulty obtaining a loan or opening a bank account, to be under-represented in corporate and public decision-making positions, and to face greater discrimination in economic and social life because of their gender.

The Strategy promoted a vision for a future for the countries where the EBRD invested:

> In which women and men, regardless of socio-economic status, have the same rights and opportunities to access finance and assets, establish and lead business, participate in decision-making processes affecting their lives and have equal and safe access to public services.

In the same way that the EBRD had endorsed the third MDG back in 2008 with a pledge to deliver a Gender Action Plan, this new EBRD Gender Strategy was also in line with the new 2030 Agenda for Sustainable Development and the SDGs that had been unveiled at the UN in September 2015. The SDG5 pledged to: "Achieve gender equality and empower all women and girls".

Announcing the Board's approval of the new Strategy on 9 December 2015, Chakrabarti said:

> The EBRD's new gender strategy is part of the Bank's response to the new Sustainable Development Goals set by the UN's 2030 Agenda. For the first time, in this agenda, goals are also set for the private sector. We will be helping our clients, in both the public and private sectors, to promote greater equality of opportunity. It is the right thing to do and it makes good business sense.[20]

Commenting on the Strategy, Bergman said:

> Numerous studies confirm the macroeconomic case for equal opportunities. But one doesn't even need to rely on these to realise that there is a need

---

20 EBRD Press release, 9 December 2015. 'EBRD adopts Gender Strategy, calls for more private sector engagement on gender equality'.

> for greater equality. Women comprise half of the world's population, half of the world's talent and capacity, and are society's driving force of survival in times of crisis. Today, no country can be competitive globally without using female talent in business, be it in the public or private sector.[21]

Looking back in 2021 on the development of the Strategy, Alistair Clark, Managing Director for Environment and Sustainability, said: "The importance of the Strategy was to move away from a compliance, non-discrimination lens towards mainstreaming of gender into the Bank's investments and indeed its internal operations. A hugely important step."[22]

7. Economic Inclusion Strategy

At the very start of the discussion of the new Gender Strategy, some Board members asked whether there would be a separate inclusion strategy. This was clearly on the agenda by the time Rambousek went back to the Board in July 2016 to deliver a further progress update on economic inclusion.

It was supported by the Transition Concept Review, where inclusion was one of the six transition qualities under discussion.[23]

In cooperation with the Gender, Environmental and Sustainability and Banking teams, Rambousek was developing a strategy which would define the Bank's approach to the inclusive transition quality, deepen the focus on economic inclusion in the context of transition and build on the existing successful inclusion model.

A concept would be presented in the autumn of 2016 and the full strategy would be ready by 2017.

Support for refugees

In her update, Rambousek also outlined how inclusion was part of the EBRD's refugee crisis response.

---

21 EBRD Press release, 9 December 2015. 'EBRD adopts Gender Strategy, calls for more private sector engagement on gender equality'.

22 Interview, 2021.

23 The Transition Concept Review was presented to the FOPC in June and was agreed by the Board in November 2016 (see Chapter 6).

Earlier that year, in February, the EBRD had announced a financing package worth up to €900 million to support private sector and infrastructure projects in some of the countries worst affected by the arrival of refugees fleeing the Syrian war.

At that time, Turkey was housing more than two million refugees from Syria alone, while in Jordan, there were an estimated 1.4 million people who had fled their homes.

The aim of the EBRD support was multi-pronged. It aimed to help the host countries deal with the huge additional pressure on infrastructure but also to support private sector development and especially small- and medium-sized enterprises, helping to strengthen domestic economies while also providing job opportunities for the refugees.

The update explained how the team was adapting the existing inclusion model to support refugees and host communities. This included the mapping of skills that were most relevant to the local economy. In the case of Gaziantep in Turkey, a major centre for refugees, this referred specifically to the textile industry.

Other steps were the expansion of private sector engagement to enhance local training, as well as supporting financial literacy for refugees and building up capacity in local banks to increase awareness of Syrians, many of whom had valuable skills, as a new market segment.

The concept for an Economic Inclusion Strategy was taken to the Board in December 2016, with a clear emphasis on responding to the challenge of inequality of opportunity that had already been highlighted in the *Transition Report 2016-2017*. It drove home the point that a deterioration in equality of opportunity reduced support for markets and democracy, with the potential to lead to costly reversals in reforms.

There was within the Board strong support for the aim of the strategy to deepen and widen the EBRD's existing inclusion activities in gender, youth and the regions.

There was a more cautious support for the possible expansion into other areas such as older people, or people with disabilities or other groups that face disproportionate barriers to economic opportunity. Directors wanted to make sure that any such extension would not dilute the efforts in the three core groups.

When the final strategy was presented to the Board for approval in May 2017, Chakrabarti put inclusion very clearly in the political context of the

day. "Economic inclusion and inequality have become defining political, social and economic issues shaping the EBRD region today," he said.[24]

The Strategy made clear that there was no longer any doubt that inclusion was now an integral part of the EBRD's transition mandate and its market economy focus.

> Economic inclusion, the opening up of economic opportunities to previously under-served social groups, is integral to achieving a transition towards sustainable market economies.
>
> An inclusive market economy ensures that anyone regardless of their gender, place of birth, socio-economic environment, age or other circumstances has full and fair access to labour markets, finance and entrepreneurship and, more generally, economic opportunity. Promoting an inclusive market-based system is therefore about efficient (human) resource allocation rather than representing a social policy choice.
>
> There is also a political dimension to inclusion, beyond its contribution to efficient markets, which is to support fair and equitable access to economic opportunity as an intrinsic value and as a key element of sustainable market economies.[25]

In 2018, Gender and Economic Inclusion were brought together into one team, with Rambousek becoming its Director on 14 February 2019. The addition of Gender to her portfolio was probably not what her colleague had had in mind when he told her back in 2012 that she needed a second string to her bow.

A lot had happened since then, though, including the delivery of 350 projects with gender or inclusion dimensions, with such projects associated with some 15 to 20 per cent of the EBRD's annual business. In 2021, she reflected on the steps that had led to this stage, making clear that crucial backing bringing inclusion into the EBRD's transition toolbox had come from the countries of operations themselves.

These countries saw the projects appearing and they liked what they saw. "In Jordan, in Central Asia, and particularly in Turkey, people were saying this is very much part of the EBRD's mission. This is important.", Rambousek said.

24 Economic Inclusion Strategy (EIS), 4 May 2017.
25 Economic Inclusion Strategy (EIS), 4 May 2017.

This had been a long journey, she said. From being a small pilot, inclusion had become a source of transition impact, a full strategy and then, from 2021, one of the top three cross-cutting priorities of the EBRD.

And inclusion assumed an even greater significance just when the Covid-19 pandemic was demonstrating how clearly society's most vulnerable are hardest hit by a crisis of this magnitude.

Crises like these were not gender neutral and women, as well as young people, were suffering disproportionately.

"Never was it more important than now to focus on inclusion and equality of opportunity", Rambousek said.

Chapter 8

Supporting Resilience and Good Governance

Introduction

As part of management's rethinking on the path of transition, following the global financial crisis, stress was laid on the role of institutions in supporting economic and social development.

The Bank stepped up efforts to bolster those institutions, taking greater steps to create an environment within which the private sector economy could flourish.

At the same time, it worked more intensely on the development of domestic markets that could fuel the sustainable growth of those economies.

Effective markets would build up resilience in the face of future exogenous shocks, while the greater emphasis on institutions helped promote a quality of governance in both the private and public sectors that would galvanise, not stifle, economic enterprise.

Indeed, financial resilience and good governance were characteristics that would become increasingly important in all countries as the decade advanced. The EBRD's role would be to promote these qualities in fostering the transition of its countries of operations towards a more sustainable future.

Twenty years on from the Bank's inauguration, it was evident that markets could function without the need for multiparty democracy, as the extraordinary rise of China showed. However, that did not lessen the importance of good governance for their effective operation.

It was also clear that markets could not carry out their function without certain institutional features being present, such as arrangements to ensure effective competition, well-designed macroeconomic and regulatory rules,

the sound application of the rule of law to business activities and central banks' careful management of access to finance.

The experiences of the EBRD's countries of operations diverged sharply in some of these respects. Countries that had joined the EU, and many of those aspiring to do so within a foreseeable timeframe—that is, most countries in the Western Balkans—had made good progress in developing better institutional underpinnings to market functioning and market behaviours.[1]

Further south and east the post-crisis picture was less promising. Here, economic factions continued to dominate, corruption was endemic and society polarised between political elites and their largely powerless populations. The core institutions that in advanced economies balanced the rights of people across different interests were decidedly weak in most less advanced transition counties, and in some were missing entirely.

The EBRD was unusual in having a political as well as an economic mandate. No other IFI had a similar remit. To become a recipient member of the EBRD, the Treaty establishing the Bank required countries to be "committed to and applying" principles of multiparty democracy, pluralism and market economics.

The exercise of the political mandate in practice manifested itself primarily in a political assessment of whether a country complied with Article 1 of the AEB as part of the country strategy process. In addition, EBRD Presidents regularly conducted important, and sometimes intensive, discussions which touched on political and other governance questions with leaders of countries of operations behind closed doors. But these high-level debates did not of themselves normally resolve the more practical problems deriving from poor governance and weak institutions seen at the operational level.

The development of the private sector in the EBRD regions was often blocked by widespread state-led corruption, mundane bureaucratic hurdles and deficient legal practices that mattered to business, such as insolvency rules or fair opportunities to win public procurement contracts.

A *Business Environment and Enterprise Performance Survey* (BEEPS) study of MENA, for example, showed how "corruption may be deterring many firms from strategies that require engagement with public authorities, limiting their

1 See Figure 8.2 below p. 302 and *Transition Report 2019–20*, Chart 1.1, p. 14.

opportunities".[2] More generally, there was often a lack of basic understanding of how markets work among decision-makers and officials.

It was in this context that an EBRD legal transition team was able to provide valuable assistance. It had been created in the mid-1990s. But now, with a post-crisis focus on the need to improve institutional quality high on the agenda, its work accelerated.

The legal work covered a multitude of issues, but chief among them was an effort to raise legal and regulatory standards and improve the business environment.

As Bank operations picked up pace, and as economies developed, increased attention was paid to strengthening corporate governance, which was poor in many countries of operations. It was only after the first phase of economic development, as small family-run businesses grew larger, that many company owners began to realise the importance of good governance to the future success of their businesses.

Bad corporate practices and corruption not only hampered the smooth evolution of markets but also prevented the banking side of the EBRD from following up potentially valuable deals. Programmes for improvement could strengthen investors' appetite to provide growth capital and other finance. In the worst cases, often concerning state-owned enterprises, the EBRD was able to offer finance conditional on wider improvements to governance as a way of furthering the transition.

The focus on institutions also received input from a different direction. The original team of political counsellors based in OCE was expanded to include governance experts. The larger group, later spun off from OCE to become the Governance and Political Affairs (GPA) team, developed initiatives aimed at governance at the national policy level and sought more general improvements to the investment climate.

Efforts on better governance by the legal transition and governance teams, who worked closely together, contributed to unlocking institutional impediments to transition progress. They were supported by Chakrabarti as an EBRD President who set particular store by governance matters and related policy discussions with the authorities. The debate leading up to the Transition Concept Review (see Chapter 6) helped further by making

---

2 'What's holding back the private sector in MENA? Lessons from the Enterprise Survey (2016)', https://www.enterprisesurveys.org/en/reports/mena-report.

clear, including to bankers pursuing investments, that 'well-governed' was an important quality which needed to be in place for a successful transition to a sustainable market economy.

A second stream of work that also received significantly greater attention after the financial crisis, again as a result of the 'learning from the past' process, concerned local currency and capital market development. Like the pursuit of better governance, it was not a new subject for the EBRD. The goal of improving capital markets in the EBRD region, and lending in local currency for operations, had been there from the beginning.

However, clients' desire for foreign currency had proved to be addictive in the boom times of the early 2000s—a dependency picked out later at one memorable Operations Committee meeting by a senior Committee member confronting an astonished team, who were proposing a foreign currency loan to a client ahead of an all-too-likely devaluation: "Don't sell them more of these FX drugs. Yes, I mean it, D-R-U-G-S!"

When the crisis came the result for those holding Japanese yen or Swiss franc mortgages was indeed very painful. If an excessive dependency on foreign currency lending was not to happen again—and with the rapid cooling on new transactions on the part of foreign financiers—local capital markets needed to be able to facilitate better the intermediation of domestic savings and make local finance more easily available for investment. The EBRD too needed to be able to offer a wider range of competitive local currency financial products.

This prompted a move, led by the Chief Economist and Treasury departments in 2010, to create a small cross-departmental team and the preparation of what became the first comprehensive initiative, and later strategy, by the EBRD on Local Currency and Capital Markets.

The work tied in with the analysis being done under the Vienna Initiative where regulators, the European Commission and several IFIs were similarly concerned with the failures of capital markets that had been seen in the global and European financial crises.

The internal mix of economists and financial markets' specialists grew to become a self-standing team, interacting with the Banking and Treasury departments to facilitate projects and technical assistance in several areas.

The core of the work was designed to build up the resilience of countries of operations against financial shocks, one of the transition qualities that acquired greater prominence after the crisis.

Much of the work was directed at weaker transition countries, where it concentrated on improving market infrastructure and the proper sequencing of reforms, starting with better functioning money markets and developing interest rate benchmarks, as well as on the provision of local currency through Bank operations to help smaller businesses less able to access finance from banks.

But there was also work in the advanced transition countries to introduce more sophisticated capital market instruments and mechanisms seen in more developed markets, such as covered bonds, electronic trading platforms and robust company listing arrangements.

This chapter looks at how the EBRD supported resilience and good governance in its countries of operations, two qualities captured by the Transition Concept Review, and the way this played out in practice through the efforts of the Bank, notably during the decade or so after the global financial crisis.

I. STRENGTHENING ECONOMIC RESILIENCE

1. The Role of Financial Markets

"Capital markets are the engine rooms of modern economies," Chakrabarti said at the 2018 launch of the EBRD's Strategy for Local Currency and Capital Markets Development. "They help to mobilise and price capital, as well as mitigate risks", he added.[3]

Capital market development was one of the key elements in the EBRD's efforts to deliver resilience, especially in the face of external shocks. The focus on resilience had increased since the financial crises at the turn of the decade.

The Bank had launched a Local Currency and Local Capital Market Development (LC2) initiative in 2010 as a direct result of vulnerabilities that had been unmasked by the 2008-2009 global financial crisis, particularly an overdependence on foreign exchange (FX) borrowing in its countries of operations.

The 2010 initiative provided substance and a systematic approach to a priority that the EBRD's founders had established from the Bank's earliest days. The Agreement Establishing the Bank expressly provided that it was a

3 'Local Currency and Capital Markets (LC2) Strategy 2019–2024', 29 November 2018.

function of the EBRD "to stimulate and encourage the development of capital markets".[4]

As western equity and debt capital markets became increasingly sophisticated, the Bank worked to share these developments with its countries of operations and help them create or deepen their own markets and to diversify risks.

For many countries of operations, it was the money market that needed attention first. Without efficient interbank and treasury bill markets longer term local debt capital markets would not be able to emerge. Economic instabilities in these countries, together with weaknesses in their financial markets, also led to reliance on foreign currency over domestic currency. These factors hampered local financial market development and posed additional risks to financial stability. The EBRD paid particular attention to the underlying causes of these problems and ways to alleviate them.

Over the decades there was solid progress in building up financial markets in most countries of operations, helped by the gearing up of activities after the global and EU financial crises. The Bank was instrumental in bringing forward changes that helped financial intermediation work more effectively, allowing countries to step up to the next level and add to the supply of finance through capital markets. The EBRD was an important and influential force, taking a pioneering role in many market milestones.

Thirty years after the signing of the AEB, as demand for finance by private enterprises rose rapidly as a consequence of the Covid-19 pandemic, an even more intense focus was thrown on the vital need for well-functioning, efficient and transparent financial markets. Demand for capital was rising sharply as finance from all available sources—including from capital markets—was needed to fund cash shortfalls and a post-crisis recovery.

There was still more to be done to address vulnerabilities and deepen financial markets to support a more resilient economic future, even in the capital markets of the EBRD's most advanced economies.

Foreign or local currency?

However axiomatic the promotion of effective financial markets may have seemed to the early supporters of the EBRD—and perhaps especially so from

4 Article 2 (v) of the AEB.

the EBRD Headquarters in the heart of the City of London—the goal had not always been so eagerly embraced by the EBRD's countries of operations.

As became apparent during the global financial crisis, some of the blame for an earlier reluctance to build local capital markets fell on the EBRD itself for so actively—and so successfully—promoting a development model that relied on a dominant banking system and inflows of foreign investment in hard currency.

In its early lending to banks and domestic corporates—such as in Russia where clients preferred to operate in US dollars—the Bank's business activities were almost entirely conducted in the US dollar and the euro and its precursor, the ECU.

At the same time, there were many apparently financially rational arguments for clients borrowing money at low interest rates in currencies managed by institutionally robust foreign central banks.

What was the balance of risks between local and foreign currency lending and borrowing?

The EBRD perspective

From the EBRD's point of view, there were good arguments in principle from the beginning for lending and borrowing in local currency to support its operations.

Lending in local currency would reduce unhedged currency mismatches on the balance sheets of corporate and household sectors and extend the maturity of local currency loans available in the market—reinforcing market indices (or creating new ones). Short-term liquidity would return to the domestic economy and the Bank could reduce its exposure to FX risks in projects that generated local currency income and thereby improve their creditworthiness.

By borrowing in local currency, the EBRD could offer a triple-A benchmark as an alternative to the government yield curve, which would increase the transparency of corporate pricing in the domestic market and strengthen market indices, and EBRD debt instruments created an opportunity for credit diversification in domestic investors' portfolios (and a conduit for international investors).

In practice, however, the Bank experienced difficulties in funding local currency: its offer was limited, demand was weak relative to FX and it was

expensive to arrange and manage. There was strong and growing demand for lending in FX, and with the EBRD's predominantly hard currency balance sheet requiring matched currency and interest rate risks, local currency matters did not command significant management attention at that time.

Early days of local currency and capital market development

The EBRD's first tangible example of support for market development was a local currency bond the Bank issued in Hungary in 1994. The funds were used to finance a local currency investment in a Hungarian motorway.

Other issues followed that five-year, inflation-linked forint bond, and in the next eight years EBRD bonds also appeared denominated in the Czech, Estonian, Polish, Russian, and Slovak currencies. The first steps had been taken. More widely, outstanding local corporate bond issues in emerging markets increased nearly tenfold between the late 1990s and 2003.

By 2006, the Bank had also made loans in eight domestic currencies: the Polish zloty, the Russian rouble, the Hungarian forint, the Romanian leu, the Czech koruna, the Bulgarian lev, the Slovak koruna, and the Kazakh tenge.

Extending the Bank's ability to lend in local currency had some particular transition advantages: it allowed banks to on-lend to riskier sub-borrowers, such as SMEs without foreign currency earnings; it mitigated currency mismatches for corporate borrowers, reducing balance sheet risks and funding costs, allowing room for more investment; and with public sector utilities in several countries legally barred from borrowing in foreign currency, it widened the scope for the Bank's engagement in the municipal infrastructure sector.

A report[5] by the EBRD's Treasury and Economics departments published in 2006 underlined the challenges and pitfalls involved in carrying out this complex mission.

The findings reminded readers that previous crises had underlined the importance of diversifying the funding of the private sector away from foreign currency sources, and from short-term domestic bank finance that was also prone to disruptions.

The EBRD's interventions were meant to help advance local bond markets so they would ultimately become sustainable without IFI involvement,

5 'Local Currency Operations of the EBRD – Information Memorandum Presentation to Directors', 20 October 2006.

in line with the EBRD's overall transition mandate—only being there when it is needed.

However, the report warned: "The experience has been that developing liquid local bond markets in transition countries is a process that requires lengthy and costly reform of financial regulations and institutions."

It was, moreover, by no means clear that such markets would ever become viable in those countries that lacked a liquid banking system or where financial transactions were largely conducted in a foreign currency.

Given the havoc that overdependence on foreign currency borrowing would wreak on EBRD countries of operations during the crisis two years later, the report was percipient.

It noted that currency mismatches on the balance sheets of corporates and households in transition countries had grown following a period of relative exchange rate stability. Banks in these countries had rapidly expanded the stock of their loans denominated in foreign currency, typically but not exclusively in euro or US dollars.

The authors pointed to the lessons of experience elsewhere:

> Recent financial crises, most notably in Uruguay in 2002, have underlined that currency mismatches can be an important vulnerability of the financial system ... Balance sheet risks—in terms of currency or maturity mismatches—have proven to be one of the most debilitating features of rapid financial development, with the potential to set growth and poverty reduction back by many years.[6]

In these early days, local currency bonds were mostly issued in order to raise funding for local currency lending, including by the EBRD, and targeted international investors. These debt instruments were settled off-shore and often listed on the London Stock Exchange, which had the advantage of keeping costs and bureaucracy low.

While valuable in their own right, these operations did not generally support the wider development of domestic capital markets and a more comprehensive solution was needed.

---

6 'Local Currency Operations of the EBRD–Information Memorandum Presentation to Directors', 20 October 2006.

MosPrime: a benchmark index that supported capital market development

The Bank issued three domestic rouble bonds in 2005 and 2006 that played an important role in the development of the Russian capital market. The five-year floating rate notes worth a total of 17.5 billion roubles provided the benchmark in the market, as the country's first international triple-A issue.

Much more significant, however, had been the extensive legal and regulatory dialogue between the EBRD and the Russian authorities, involving amendments to 13 laws, to arrive at this stage. The Bank had been working with Moscow since 1999 providing the technical and legal expertise needed to develop a framework for long-term local currency bond issues.

This had led to a new Securities Market Law in 2003, the registration of disclosure regulations for IFIs in Russia, the creation of listing regulations for bonds from foreign issuers and there was now provision for EBRD issues to be eligible for repurchase deals with the Russian central bank.

Finally, and perhaps most visibly, extensive negotiation between the EBRD and Russia's National Currency Association led to the creation of a new money-market index, the Moscow Prime Offered Rate, MosPrime.

Launched in 2005, MosPrime, was based on the yield for money-market time deposits offered by first-tier banks in the Russian market to financial institutions of comparable credit standing. It quickly became a credible benchmark index and provided a high level of transparency and consistency in pricing. It allowed the interbank money-market to develop greater liquidity, making it more efficient, and eventually led to longer maturities of interbank money market transactions.

To add to its credibility, the EBRD priced all of its domestic Russian bonds off MosPrime and promoted MosPrime pricing as a credible benchmark for commercial loans and local currency bond issues by entities other than IFIs.

In 2006, the EBRD used MosPrime as a benchmark when it syndicated rouble loans to Mosenergo, the Russian power generation company, and Hydro-OGK, the hydropower company. The loans extended the tenors on corporate debt to up to 10 years and helped encourage commercial banks to enter the market.

In 2009, at the height of the global financial crisis, high rates for the MosPrime index as well as unwelcome volatility caused concerns for borrowers. The response from the Russian authorities was to provide the index

with more institutional support and the EBRD pledged to help further deepen and strengthen it.

Following the successful introduction of MosPrime, similar benchmarks developed with the EBRD's help soon appeared in Ukraine with KievPrime,[7] and in Kazakhstan with KazPrime.[8]

The dangers of excessive FX exposure

Even as the EBRD worked to gain access to finance in local currencies and to pass on the funds in domestic loans, the appetite for low interest rate foreign credit continued unabated.

Potential clients for local currency funding often found the terms uncompetitive[9] or they fixated on the interest rate differential and disregarded possible currency risks of foreign borrowing.

There was a logic to the reluctances, especially in less advanced transition countries. Potential borrowers were concerned about volatile domestic interest rates that reflected macroeconomic, and sometimes political, instability. There was little or no opportunity to hedge risks and the domestic pricing mechanism was less transparent than in the larger, more liquid markets. Weak market infrastructure posed settlement risks on top of the pricing and rollover risks.

The shift toward the heavy reliance on foreign currency debt further accelerated after eight of the EBRD's countries of operations joined the EU in 2004.

As mortgage markets developed in the Baltic States and elsewhere, they were denominated almost entirely in foreign currencies.

In Hungary, hundreds of thousands of FX mortgages were taken out, and by 2008 they accounted for 75 per cent of the total portfolio, compared with just 16 per cent in 2004. Many of the mortgages were in euros, but the overwhelming majority were in Swiss francs.

During the heady days of growth around the middle of the decade, and buoyed by optimism linked to EU access, there seemed to be little risk.

---

7 Joanna Chung, 'KievPrime index set to ease lending', *Financial Times*, 12 November 2007, https://www.ft.com/content/c01a4724-9145-11dc-9590-0000779fd2ac.

8 EBRD *Transition Report 2007*, p. 142.

9 Limited choice and weak regulation in many countries meant banks were able to obtain local deposits at well below base rates while weak competition and high inflation allowed them to charge borrowers high interest rates.

And the prospect of cheap funding to finance aspirational lifestyles was appealing.

As the EBRD's *Transition Report 2010* explained, Hungary stood out with a particularly large gap between domestic and foreign borrowing rates.

A Hungarian household taking out a one-year consumer loan in forints in early 2006 would have been charged interest of about 22 per cent. With inflation running at an annual rate of eight per cent at the start of 2007, the real interest rate paid on the local loan would have been around 14 per cent. The borrower would have paid about seven per cent interest on the same credit in euros which, based on the Hungarian inflation rate and a roughly unchanged euro-forint exchange rate over the year, implied a real interest rate of close to zero.

There was of course an economic reason for high domestic interest rates.

In the case of Hungary, they reflected the real possibility of a currency crash and a spike in inflation. An IMF mission to Hungary in 2006 had warned "the state of public finances—epitomised by endemic deficit overshooting—is undermining economic stability and growth prospects" and pointed to "the risk of a fiscally-induced crisis".[10] The *Transition Report* noted that "consumers borrowing in forints would have been protected from the consequences of such a crash, while consumers borrowing in euros would have seen the local currency value of their debts rise sharply."[11]

After a long period when the risks had been ignored, the dangers did emerge dramatically as soon as the global and euro area crises struck and currencies in central and eastern Europe came under pressure.

The Hungarian forint lost 66 per cent of its value against the Swiss franc between September 2008 and November 2011, driving the cost of those mortgages and other loans sharply higher and leaving thousands of homeowners in arrears and many in financial distress.

The consequences were long-lasting. As part of a populist move against the banks (most of which were foreign-owned), the government of Viktor Orbán launched a debt relief scheme for FX borrowers in 2011 that allowed mortgage holders to repay their loans at a discount to market rates.

---

10 IMF Press release, 6 June 2006. Hungary - 2006 Article IV Consultation, Concluding Statement of the IMF Mission, 6 June 2006, https://www.imf.org/en/News/Articles/2015/09/28/04/52/mcs060606

11 EBRD *Transition Report 2010*, p. 50.

"I do not want to live in a country ... where one million people must live in debt slavery ... I will change this," Orbán told a radio programme,[12] adding that the banks had to bear two-thirds of the cost of the programme.[13]

The Hungarian measures provoked an angry response, especially from neighbouring Austria, home to many of the mortgage lenders.

A reassessment of the financial development model

The EBRD's 2009 *Transition Report*, issued in November of that year, took a long, hard look at the development model for the transition region. This model, as Chief Economist Erik Berglof said in his foreword, had "cut both ways".[14] The very close economic ties with more advanced countries and a financial dependence on them had made many transition countries highly susceptible to the crisis in the West.

It was, however, precisely those links that had managed to mitigate the impact of capital outflows, help develop more mature institutions and also galvanise international support just when it was most needed. "For all these reasons, this crisis has not spiralled out of control," Berglof said.

Nevertheless, that double-edged development sword had been particularly apparent in the financial sectors of the EBRD's countries of operations. Financial integration had led to excessive private sector credit growth and excessive private sector debt levels. Berglof continued:

> It is also likely to have encouraged indebtedness in foreign currency, which has complicated the crisis in many countries. The lesson from this experience is not to attempt to reverse financial integration—that would be both unfeasible and unwise—but to mitigate its risks, particularly through policy frameworks and institutional development that address the problem of foreign currency lending and that lead to a better management of future booms.

---

12 *Reuters*, 28 October 2011. 'Hungary PM will save Hungarians from FX debt "slavery"'.

13 Further measures were taken against the banks in the following years, including a Borrowers' Refund Scheme in 2014.

14 EBRD *Transition Report 2009*, Foreword.

The need for a more robust framework

While the *Transition Report* concluded it would be wrong to reverse or fundamentally change the development model there were a number of key policy conclusions that had to be drawn. One of these was that: "The transition region must deal with the bias toward FX lending, which could continue to pose a threat to stability."

The available evidence suggested the need for a three-pronged strategy.

First, it was important to build credible macroeconomic frameworks and institutions that focused on stable inflation and allowed exchange rate flexibility, where that was possible.

Second, local currency money and bond markets had to be developed in a systematic fashion, with limited subsidy, in order to extend the sources of domestic funding and make it easier to price domestic currency loans at longer maturities.

And third, there had to be regulation that limited foreign currency exposure in the banking, corporate and household sectors.

The report made clear that the first condition was a *sine qua non* of the process. A credible macroeconomic framework and low inflation volatility were preconditions for local currency market development. Without them, local issuance with longer maturities would be prohibitively expensive. Furthermore, any form of regulation that put a limit on foreign currency exposure would make no sense if that foreign borrowing were a response to an environment of volatile domestic inflation.

Regulation had plenty of useful roles to play, especially in the more advanced countries with stronger institutions. But in less advanced economies, there could be no substitute for tackling the most basic economic problems:

> Less advanced transition countries in which macroeconomic institutions are relatively weak need to focus above all on strengthening their fiscal frameworks and enhancing the credibility of their monetary policy institutions.

2. The Local Currency and Local Capital Markets Development Initiative

The 2009 *Transition Report* was a prelude to the launch in 2010 at the EBRD's Annual Meeting in Zagreb of the Local Currency and Local Capital Market

Development (LC2) Initiative that was a collective enterprise on the part of Banking, Legal Transition, OCE and Treasury.

The LC2 Initiative was an important part of the EBRD's response to the global financial crisis and the weaknesses in the system that it had unmasked.

Vulnerabilities due to FX lending combined with poor standards of information and credit assessment were now clearly visible. Unsustainable external imbalances were widely recognised.

Significantly, the new initiative made the point that local capital markets development had to be a priority even for those countries on their way to becoming members of the eurozone.

The EBRD countries of operations that had joined the EU in 2004 and 2007 had also signed up to adopt the euro, whenever the conditions were right. Some market commentators at the time said this had led to capital markets lethargy, as euro membership was seen as some sort of panacea for problems linked to raising capital safely.

But the EBRD initiative made clear that this capital markets development work "even for eventual eurozone members [is] <u>not</u> a detour".[15]

What was clear as the initiative got underway was that the response to the lack of appetite for local currency borrowing was a much bigger exercise than just making local currency available.

The Bank and its partners needed to focus on all the factors that explained the lack of local currency and capital markets development, including the histories of inflation volatility and lack of macroeconomic credibility and the inadequate market infrastructure. It had to address a poorly regulated and undercapitalised banking system, as well as institutional and legal weaknesses.

It was also important to take into account vast differences that prevailed across all of the EBRD regions at this time. There was no one-solution-fits-all for economies which had attained very different levels of market sophistication—or no market sophistication at all.

The main contribution the EBRD could make lay in its unique combination of a role in promoting sound policies in the region and the operational demands of providing investment capital.

Under the initiative, it would establish a diagnostic framework that would identify obstacles to capital markets development and local currency funding and lending.

---

15 'Local Currency and Local Capital Markets Development Initiative', May 2010.

It would work together with governments, partner IFIs and the private sector to provide technical and policy advice, especially in the legal and regulatory area and on market infrastructure. It would be predicated on evidence of government commitments to macroeconomic stability.

It would continue to strengthen risk management and the capitalisation of the banking sector.

It would undertake its own local currency funding to support the development of the markets as well as EBRD projects.

It would develop demand for local currency assets from domestic institutions by actively supporting pension funds and insurance sector development and, in coordination with other investing IFIs, it would work to "make markets" in the domestic currencies.

The initiative broadened the EBRD's approach. Whereas previously the Bank had primarily focused on reforms that would allow EBRD funding and lending in local currency, the focus now was on actions that benefitted the development of local capital markets and local currency funding.

Specifically, in the less advanced transition countries the focus—with guidance from the IMF—would be on trying to change inflation expectations, adopting a consistent approach to the use of local currency and helping to shift sovereign debt management towards domestic funding sources.

One priority was to ensure that any foreign exchange regulation aimed at discouraging the use of foreign currency borrowing made economic sense and did not just end up cutting the economy off from all sources of credit.

Launching the initiative at the EBRD Annual Meeting in Zagreb, Berglof, said:

> The crisis laid bare the region's twin vulnerabilities of excessive reliance on foreign capital and excessive use of foreign exchange borrowing. As the recovery takes hold in the region, it is important to urgently address these vulnerabilities, with a fresh eye and approach that fuses the knowledge and expertise of key stakeholders: governments, IFIs, the banks and other private sector stakeholders.[16]

16 EBRD Press release. 15 May 2010. 'EBRD launches local currency and local capital markets initiative'.

The Vienna Initiative's role

The new initiative put a significant emphasis on a collective response that involved all of the major international financial institutions. Already ahead of the launch, in a drive led by the EBRD, officials involved in the Vienna Initiative,[17] the private-public platform that had been established to coordinate the response of market participants to the immediate impact of the global financial crisis, were working on a plan.

In March 2010, Piroska Nagy-Mohácsi, EBRD Director of Country Economics and Policy and a driving force of the first iteration of the Vienna Initiative, delivered a call for action to a meeting of the Vienna Initiative in Athens as it contemplated a new phase, Vienna Plus.

She laid out the problems that had arisen from currency and capital markets weaknesses in a positive way, stressing that strong and sustained growth in emerging Europe was in the interest of every stakeholder present. The "time is right", she said, to address the region's twin vulnerabilities: excessive reliance on foreign capital and FX lending to unhedged borrowers. Efforts had to be directed towards "reforming the growth model".

This was a problem to which the Vienna Plus community could respond. It needed to be fixed and there was a road map. "Let's do it!" was Nagy-Mohácsi's appeal to the group.[18]

The EBRD led what was to become the Vienna Initiative Working Group on Local Currency and Capital Markets Development, whose report was formally approved by a Full Forum Meeting in March 2011 in Brussels.[19]

The Working Group came up with a division of labour between the key stakeholders in the local currency debate: the authorities in the regions, the banks and the IFIs.

It was the responsibility of the authorities primarily to ensure macroeconomic stability and a low inflation environment. However, there was also a need for them to address the risks of foreign currency exposure to borrowers without foreign currency income.

---

17 See Chapter 2.

18 Piroska Nagy-Mohácsi, EBRD. 'Addressing Emerging Europe's Vulnerabilities: Weak Domestic Markets and Excessive Forex Exposures. A Coordinated Approach', Vienna Plus European Bank Coordination ("Vienna") Meeting, Athens, 19 March 2010.

19 Report by the Public-Private Sector Working Group on Local Currency and Capital Market Development, 16-17 March 2011, Brussels,

Banks had to strengthen risk management procedures to take into account the higher credit risk of unhedged borrowers in foreign currency. Other steps included proposals that they discontinue the riskiest forms of foreign currency lending to unhedged borrowers and that they themselves proactively participate in local currency funding.

It was up to IFIs, including the EBRD, to coordinate their support for governments in their pursuit of policies conducive to the use of local currency and in the development of local capital markets, "according to their remit and expertise".

For investing IFIs like the EBRD, this included helping develop local currency longer-term funding instruments and markets, the investor base (pension and insurance funds) and lending in local currency.

The Vienna Plus effort had wide applicability but was focused very directly on the EU and its immediate neighbourhood. Further afield were EBRD countries of operations which had largely escaped the worst of the calamities that beset the main European arena but were no less vulnerable. Here, macroeconomic instabilities and weak financial market infrastructure and regulation were particularly significant and a cause of poor economic resilience. But the Bank continued to face difficulties in the provision of local currency in those markets and a further effort was needed.

Help for Early Transition Countries (ETCs)

One specific offshoot of the EBRD's 2010 LC2 initiative had been a local currency loan programme aimed at the least advanced EBRD economies, the Early Transition Countries (ETCs) in Central Asia and the Caucasus.

Their exposure to the dangers of almost exclusive borrowing in US dollars had followed local currency devaluations of up to 30 per cent that coincided with a growing risk aversion on the part of international investors towards these markets.

Most of these economies were highly dollarised and local currency interest rates were high, which reflected the significant levels of risk and limited development of their financial markets.

The particular problem facing the EBRD in lending local currency to banks and corporates in the ETCs was the high cost of funding. Sourcing these little-traded currencies was difficult and expensive, and high margins were needed on top for risk and sound banking reasons. As a result, the

EBRD local currency offer was not competitive even against local banks' lending at double digit rates.

To make headway, the Bank needed both to pursue policy dialogue with the authorities to upgrade the financial infrastructure and to be able to increase local currency lending to clients in these economies.

In February 2011, the Board approved a new programme, the ETC Local Currency Loan Programme, whereby the EBRD and each participating country would agree an MoU under which the Bank and the local authorities pledged to work together to create an environment that was conducive to local currency and capital market development. The EBRD would then follow up with lending in the local currency to financial institutions, corporates and SMEs.

The programme aimed for a better match between lending currencies and revenues to reduce insolvency risk at the micro level and to reduce the increasing systemic risk from dollarisation in the financial sector at the macro level.

The Bank was able to use a grant-funded risk facility to deliver its local currency lending to the ETC countries under the programme, with a significant reduction in its margin which allowed it to price its loans closer to market rates.

Financial support for that facility came from an ETC Local Currency Risk Sharing Special Fund that combined EBRD capital and donor grants.

Early loans under this programme included credits to micro-lending organisations in Tajikistan and the Kyrgyz Republic, boosting the availability of Tajik somoni and Kyrgyz som loans to local entrepreneurs.

By the following year, the Bank had reached agreements on local currency lending with five of the ETC countries: Armenia, Georgia, Kyrgyz Republic, Moldova and Tajikistan and management was quickly able to report real progress.

An update to the Board in April 2012 said:

> The Programme has begun to lead to a shift in the Bank's lending in the MoU Countries away from the US Dollar into local currency. Since the start of the Programme, 48 per cent of the EBRD loans signed in 2H2011 that were eligible for the Programme were signed in local currency—a significant increase over 18 per cent in 2010 and 10 per cent in 2009.[20]

20 '2012 annual report on the ETC local currency loan programme', April 2012.

The EBRD was able to support its local currency lending to ETCs via its connection with the Currency Exchange Fund (TCX), an organisation in which the EBRD was an investor and which helped hedge currency risks. The EBRD funded itself in the local currency of the relevant ETC on the back of currency swaps with TCX, a specialist in "exotic" currency hedges.

A focus on local currency lending to SMEs

By late 2015, the ETC programme had expanded to include Mongolia and was showing signs of success.

In January 2016, the Board approved a new, similar programme—the SME Local Currency Programme—that broadened the original initiative and extended it beyond the ETCs.

The new programme had three components, the first of which was EBRD-led policy dialogue and technical cooperation to improve domestic financial intermediation in local currency, supporting capacity building for central banks in areas like policy formulation.

Second, it would broaden the range of instruments that the EBRD's Treasury team was able to use to fund and hedge its local currency exposures, so as to step up further availability of local currency funding for SMEs.

The third component was a US$ 500 million Local Currency Lending Facility that would lower the premium on interest rates on EBRD SME local currency loans over domestic market rates, by reducing the Bank's margin on its loans with the help of funding from donors to provide a first-loss guarantee to the EBRD.[21]

The earlier programme had just been open to ETCs. The new facility was available to all EBRD countries of operations that did not use the euro as their local currency (de jure or de facto), and which still had transition gaps as far as MSME financing was concerned.

The number of countries signing up for the programme continued to increase and, by 2020, 15 countries were involved: Albania, Armenia, Azerbaijan, Belarus, Egypt, Georgia, Kyrgyz Republic, Moldova, Mongolia, Morocco, Serbia, Tajikistan, Tunisia, Ukraine, and Uzbekistan.

---

21 Funding came from donors to the ETC Multi-Donor Fund (active donors: Canada, Finland, Germany, Ireland, Japan, Korea, and Luxembourg), the US Treasury, Switzerland's State Secretariat for Economic Affairs (SECO) and Japan, as well as from the Shareholder Special Fund (SSF).

In December 2020, the facility was increased to US$ 600 million, in response to rising demand during the Covid-19 pandemic.

3. Raising Regulatory Standards and Capital Market Innovations

Another key element in the 2010 LC2 Initiative was the development by the EBRD's Legal Transition team of new tools to assess the relevant legal and regulatory framework in individual countries of operations.

Although the analysis revealed country-specific trends, there were common themes where the EBRD could take an advisory role, including in issuance and listing procedures, a legal framework for derivatives and repurchase agreement (repos), the insolvency treatment of bondholders and credit rating requirements.

In more advanced countries like Romania and Hungary, the development of secured products, in particular covered bonds and simple transparent securitisations, was identified as an important step.

Covered bonds

In subsequent years, the EBRD was to assume a leading role in the development of the market for covered bonds, which it saw as an important and efficient source of long-term funding for credit institutions.

In the covered bond market, banks issue mortgages to customers and these mortgages are then ring fenced and used as collateral for bonds sold to investors.

According to Jacek Kubas, who leads the innovation group of the EBRD's Capital Markets Development (CMD) team, this long-term funding tool has huge benefits for issuers, investors, market participants and the general public.

"Especially in central and eastern Europe, this has grown into an important source of stable funding," says Kubas who has been a major proponent of the instrument within the Bank. He added:

> A well-functioning covered bond market made an important contribution to more affordable housing. With this stable, fixed-term funding source, credit institutions are in a much better position to provide affordable mortgages for consumers and businesses.

The EBRD teams led the way in providing support for legal and regulatory reforms to help the development of the covered bond market in the region.

In Poland, the EBRD played an active role. In response to a request from the Polish Ministry of Finance, the Bank worked on drafting legal provisions for the new law which was approved by the Polish Parliament and entered into force on 1 January 2016.

The EBRD followed up this legal work with a 50 million zloty (approximately €12 million) investment in 2017 in the first zloty-denominated covered bond issue by PKO Bank Hipoteczny, providing PKO with access to long-term funding for its mortgage loan portfolio.

Two years later, PKO Bank became the first Polish institution to issue "green" covered bonds, where the funds were used to finance residential buildings that reduce greenhouse gas emissions and to provide a new capital market instrument for PKO to finance green mortgages.

The EBRD took part in the issue, taking up 20 per cent of the total 250 million zloty bond, in what was the first project under a new EBRD Green and Sustainability Bond investment framework targeted at financial institutions.[22]

In Romania in 2015, there had been no covered bond issuance since the adoption of a covered bond law in 2006. The EBRD played a significant advisory role in developing an updated covered bond law that was passed by the Romanian Parliament in September 2015.

As with PKO Bank in Poland, the EBRD followed its advisory support with an investment in Romania's first covered bond, taking a €40 million portion of a €200 million offering from Romania's Alpha Bank.

Similar legal support took place in the Slovak Republic, the Baltic States and Croatia.

In addition to the covered bond investments in Poland and Romania, the EBRD also supported issues in Greece, Hungary, Turkey, and the Slovak Republic.

By the end of 2020, the EBRD had invested a total of €788 million in covered bonds across its regions.

22 Green bonds are also discussed in Chapter 9.

Sequencing financial market development

The launch of the LC2 Initiative in 2010 took place alongside the EBRD's 2011–2015 strategy, Capital Resources Review 4, which placed capital market development at the very top of its list of strategic initiatives for the period. Under the rubric of Building Stable Financial Sectors, it said:

> The Bank will draw on its comparative advantage in promoting sound balance sheets and risk practices in financial institutions. More broadly, it will make a concerted effort, with other IFIs, to accelerate the development of local capital markets in order to reduce systemic vulnerabilities.[23]

In 2013, the EBRD took its engagement in this area to a new level with the elaboration of a more wide-reaching strategy. On 10 December, the Board formally endorsed the new LC2 Development Strategic Initiative.

A year earlier a designated team of experts had been created to spearhead the strategy. The role of this team (originally called LC2 and later CMD), headed initially by Estonian banker André Küüsvek, was to coordinate, support and complement the LC2 related activities of Banking, Treasury, OCE and the Office of the General Counsel, through a combination of policy dialogue, transaction design and support, and capacity building.

The strategy brought together the strands of thinking that had been developed during the first years of the original initiative. This was encapsulated in a pyramid model demonstrating the sequencing needed to support successful financial market development based on an IMF paper.[24]

Jim Turnbull, a financial markets veteran and Deputy Director in the CMD team, said the pyramid underscored the importance of proper sequencing and ongoing diagnostics in the development of capital markets. This could not be underestimated, he said: "The message is crystal clear. For it to be sustainable, only do the next level of capital market development work that is appropriate and builds on the existing level of development."[25]

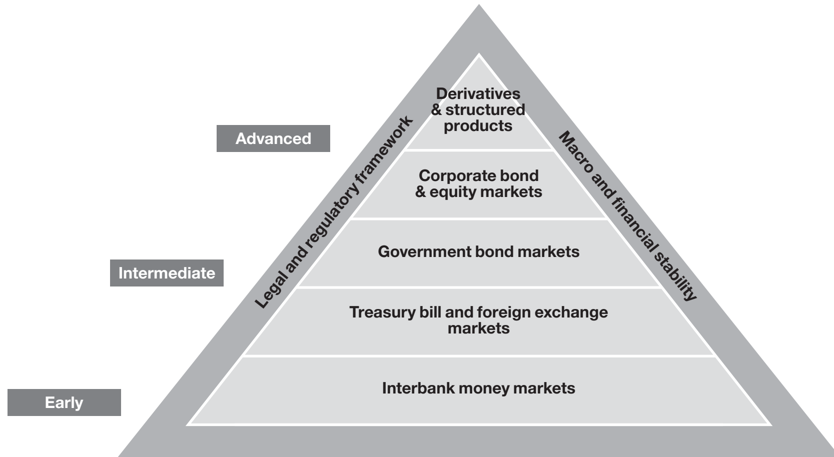
---

23 Capital Resources Review (CRR 4), President's Recommendation, p.2.

24 C. Karacadag, V. Sundararajan, and J. Elliot 'Managing Risks in Financial Market Development: The Role of Sequencing', IMF Working Paper, June 2003, WP/03/116, p. 7. https://www.elibrary.imf.org/view/journals/001/2003/116/article-A001-en.xml.

25 Interview, February 2021.

Figure 8.1 A Pyramid Model of Financial Market Development: the Karacadag-Sundararajan-Elliott Model.



Source: IMF Working Paper, No.03/116.

The team had clear objectives that were approached on a Bank-wide level, including upgrading capital markets policy frameworks, enhancing legal and regulatory environments, improving capital market infrastructure and expanding the product range and investor base across the EBRD's countries of operations.

There were in the coming years strong examples of areas where the EBRD led the way in pioneering market developments that were creating real change to strengthen financial resilience.

A pan-Baltic capital market

One specific focus was on the Baltic countries, Estonia, Latvia, and Lithuania, three EU states with relatively sophisticated markets, but whose small size was holding them back from making more progress.

The EBRD worked closely with the European Commission and the relevant local authorities to launch a pan-Baltic capital market, forging an agreement that in the first instance harmonised capital market regulation and broke down investment barriers.

An MoU to this effect was signed in November 2017, with the EBRD providing both policy support and investments in specific projects that underpinned the market development.

The support for a covered bond market in the region was just one example where the Bank helped deepen market links across the Baltics.

The Bank was also involved in dialogue with index providers, such as MSCI and FTSE-Russell, to have the Baltics States classified as an emerging market under a single rating. This would attract a larger share of passive investor capital since the markets were unclassified or classified as frontier markets due to their small size.

In 2020, the EBRD was also supporting the creation of a pan-Baltic commercial paper market that aimed to address the short-term needs of corporate borrowers who were urgently seeking alternative sources of working capital financing, because of the contraction of the banking sector following the outbreak of the coronavirus pandemic.

Capital market support for eastern Europe and the Caucasus

In the same way that the EBRD had supported the development of the covered bond market in its regions, it also worked closely with the authorities in a number of countries in successfully delivering laws and regulations governing the use of derivatives that aimed to deepen the markets and allow more effective hedging of market risks.

Already in 2016, the Armenian parliament passed a package of laws on the financial markets, described by the then head of the EBRD's Yerevan operations, Mark Davis, as a "milestone". The EBRD had provided technical cooperation to support the drafting of the legislation, complex work involving amendments to 17 laws and the introduction of 15 new ones. The new rules provided for the enforceability of derivatives transactions, including "netting and close-out netting"—mechanisms for reducing risks associated with derivatives deals.

The EBRD worked for nine years with the Ukrainian authorities on a law passed in June 2020 that created the legal and regulatory framework for derivatives, helping Ukrainian entities such as banks, farmers and manufacturers, to hedge their foreign exchange exposures.

The Georgian parliament passed new financial market laws in early 2020, with the EBRD again helping with drafting and capacity building exercises, in coordination with the International Swaps and Derivatives Association (ISDA).

Before this, the EBRD had notched up a series of firsts on the Georgian capital markets. In March 2014, the EBRD launched the first ever bond

issued by an IFI in Georgian lari, a key step in securing the local currency for local transactions. Then, in April 2017, the EBRD issued its first Eurobond denominated and settled in lari; and in July of the same year, the EBRD took part in the first secured corporate bond denominated in lari, a first both for Georgia and the wider Caucasus region.

Capital markets innovations and linkages with transition goals

There were many other examples of the EBRD's pioneering role in individual projects.

In 2020, the EBRD invested in the first green bond issue in Greece, a €500 million offering from National Bank of Greece (NBG).

The bond was aligned with the International Capital Market Association's (ICMA) Green Bond Principles, which recommend transparency and disclosure, and promoted integrity in the development of the green bond market.

Another transaction that combined the EBRD's commitments to capital market development and low carbon transition was an investment in Poland in November 2020 in the first 'energy transition' linked bond from one of the country's largest energy companies. The Bank signed up to 24 per cent of a 1 billion zloty bond issued by the Tauron group to support its decarbonisation strategy.

This was not a 'green bond' but an issue that helped Tauron implement an ambitious strategy to reduce its carbon footprint. The company was planning a fundamental shift away from coal-based electricity generation, by closing down coal capacity, expanding its renewable portfolio of wind and solar over the coming years and investing in its distribution network so it could absorb more intermittent renewable energy generation.

With the 'transition bond', Tauron was making a clear signal of a change in direction to investors and stakeholders by including in the bond terms formal commitments to cut its CO_2 emission intensity and increase renewables capacity. It was the first time a Polish utility had issued a bond with such commitments, explicitly targeting decarbonisation investments.

Another element in this particular issue was that it was an important step in the EBRD's Just Transition Initiative, which aims to provide social protection to economies as they move away from high-carbon energy generation.[26]

26 See 'The EBRD Just Transition Initiative', June 2020, https://www.ebrd.com/just-transition.

Tauron's operations are primarily located in Silesia, the largest producer of hard coal in Europe, where mining employs 80,000 workers, or about five per cent of the regional workforce. One of the covenants in the bond issue committed Tauron to a programme to address the social impacts of closing coal generation operations.

Similarly, in Turkey, the EBRD tied a capital market innovation to an investment in the largest local energy company, Enerjisa Enerji. In August 2017, the Bank invested 100 million Turkish lira (€24 million) in an inflation-linked bond from Enerjisa Enerji. This was the EBRD's first investment in an issue linked to a consumer price index. At five years, the issue had the longest tenor for a local currency instrument from a Turkish company.

Local currency borrowing is particularly important for utilities where revenues are usually overwhelmingly denominated in that currency. However, the CPI link was an added benefit for distribution companies like Enerjisa Enerji, whose revenues are also often tied to the inflation rate.

In the municipal bond sector, the EBRD supported a ground-breaking issuance by the City of Bucharest in 2015. A single maturing Eurobond which increased both currency and refinancing risk to the City, was replaced by four local currency benchmark issues with maturities of three, five, seven and 10 years—immediately resulting in a local currency yield curve benchmark for pricing municipal debt in the country. The EBRD participated in the seven and 10-year tranches to build investor confidence in longer dated issuance.

A further local currency transaction followed in Croatia where Zagreb Holding issued a local currency municipal bond which was largely purchased by local pension funds.

Stock exchanges

During this period, the EBRD also looked to increase its influence on stock market developments by directly investing in in some exchanges, where the status of shareholder allowed the Bank to nominate candidates for election to the boards of directors and seek improvements in corporate governance.

It had already in 2012 bought a 6.29 per cent stake in Russia's MICEX-RTS stock exchange, a holding it continued to maintain, despite the lack of new investment by the EBRD in Russia since 2014.

In 2015, the EBRD took a 10 per cent stake in Borsa Istanbul, only to sell it four years later following a disagreement over the appointment of a new CEO.

The EBRD still has holdings in the Bucharest stock exchange, the largest bourse in south-eastern Europe, which it bought in 2014, and in the Zagreb stock exchange, which it acquired in 2016.

In a separate development in south-eastern Europe, the EBRD played an important role in the development of SEE Link, an innovative platform that, initially, united the Bulgarian, Croatian and Macedonian stock exchanges. The three exchanges set up the SEE Link company, based in Skopje, in May 2014 and the platform became fully operational with the launch in March 2016 of an order routing system that the EBRD helped establish with a €540,000 grant.

SEE Link also created its own indices, which aimed to give the markets more visibility and greater transparency. The initial three members were subsequently joined by bourses from Belgrade and Ljubljana in December 2016, and Banja Luka and Sarajevo in August 2017.

In 2020, the EBRD teamed up with the investment bank Wood and Company to launch a dedicated research programme for SMEs listed on the exchanges of six south-eastern European economies, in Bulgaria, Croatia, North Macedonia, Romania, Serbia, and Slovenia.

At the launch of the research programme, Ivana Gažić, President of the Management Board, Zagreb Stock Exchange (ZSE), said the programme was a logical next step for the development of the SEE Link area of operations. "The lack of information about companies is often the main obstacle to making investment decisions and discovering the region's potential," she said. [27]

Kubas noted that even though an important step had been taken to give these markets scale by bringing them together on a single platform, more work was needed to increase trading volumes, with further development in the individual jurisdictions and an integrated post-trading structure.[28]

27 EBRD Press release, 20 May 2020. 'EBRD and partners launch SME equity research programme'.
28 Interview, February 2021.

4. EBRD Treasury and Markets Development

Local currency

Axel van Nederveen, a Dutch capital markets expert and EBRD Treasurer since 2004, has overall responsibility for the Bank's Treasury and funding operations and liquidity management. Treasury plays a key role in financial markets development, especially through funding local currencies and on the money market side.

Van Nederveen argues that the international development community could do more to develop local currency finance, even though there has been an increased awareness of its importance, and the challenges, since the 2009 crisis.

In a 2019 paper,[29] Aude Pacatte, Head of Portfolio Management, and van Nederveen said that issuance of local currency bonds per se by international institutions was not the panacea to unlock local currency lending and local financial markets development that they were supposed to be.

Quite often, the proceeds of such bonds had been used as relatively cheap arbitrage opportunities via swaps back into hard currency, rather than for on-lending to companies that needed access to sources of local currency. They argued that the focus should be on the development of local financial markets "in a more holistic manner" and concentrate, as in the EBRD's case, "first and foremost on creating a local currency loan offering that is in the best interests of our clients".

This could be accomplished by overcoming capacity constraints and offering wider advice than just securities market law reform. They wrote of the EBRD's approach:

> To overcome the issues of lack of capacity to borrow local currency and timing mismatches between investor demands and borrowers, we borrow from [the] domestic investor pool, by and large banks, on a floating rate basis ... This ... accommodate[s] clients' needs in terms of interest rate and maturity.

The fundamental advantage to this method, said the authors, which distinguishes it from the more restrictive, traditional back-to-back approach, is that "we are ready to manage risks on our balance sheet to borrow and

29 A. van Nederveen and A. Pacatte, 'Local currency finance: Development must or nice to have?', July 2019.

on-lend at different times in different forms". This means: "We have the willingness and capacity to bridge market gaps or imperfections by absorbing the associated risks within our balance sheet."

Turning to advice and other capacity improvements, van Nederveen and Pacatte suggested many factors were needed to increase local currency financing, including better macro frameworks, legal changes that supported new products and improved market infrastructure. They insisted that operating as a market participant in local markets, as the EBRD does routinely, made a significant difference.

The Treasury paper listed the obstacles in the way of capital market development, including high domestic interest rates, incomplete legal frameworks and the failure of banks to provide a diverse range of products.

It also highlighted the lack of an analytical toolbox, referring to the fact that the international community had not agreed clear understandings on the specific state of development of any particular market or what the next logical development steps might be, leaving governments "inundated with conflicting advice".

In response to this challenge, the EBRD developed a money market diagnostic framework in cooperation with the financial markets' development company, Frontclear, which it used in a number of countries, contracting the consulting firm OGResearch to run the diagnostics.

The framework measured money market development across a series of different criteria, providing a much clearer assessment of gaps compared with the "best of class" markets and facilitating the choice of optimum responses. By 2021, OGResearch was running diagnostic assessments in Armenia, Azerbaijan, Belarus, Egypt, Jordan, Mongolia, Morocco, Russia, and Uzbekistan.

The EBRD combined the diagnostic with Money Market Working Groups (MMWGs) which bring together the major banks and the central bank and the EBRD as an advisor. It is up to the working groups to use the results of the diagnostic framework to formulate the next logical financial market development steps.

Money markets

The original purpose of the MMWGs had been to help in the reform of money market benchmarks or the creation of such mechanisms where they did not already exist.

In just the same way that the EBRD Treasury department had helped with the creation of the MosPrime benchmark in Russia in 2005, it was also instrumental in establishing new money market benchmarks in a number of countries of operations.

The Bank had supported the calculation of the Rouble Overnight Index Average (RUONIA) that Russia introduced in 2010 and then worked with the Russian monetary authorities in subsequent years on further developments. In line with its policy of making transactions in the markets that it helps create or promote—having "skin in the game"—the EBRD traded the first rouble Overnight Interest Rate Swap after the RUONIA launch.

It subsequently also issued Eurobonds linked to ROISfix, an index of fixed interest rates for which RUONIA was the underlying instrument and inaugurated a rouble interest rate swap derivative also based on ROISfix.

More recently, the EBRD worked in cooperation with the authorities in its countries of operations on money market benchmarks in line with reforms for major currencies in other jurisdictions, in preparation for the switch to "risk-free rates" (RFRs) from the London Interbank Offered Rate (LIBOR), such as SONIA in the United Kingdom, or EONIA in the eurozone.

The EBRD assisted with the methodology for Georgia's Tbilisi Inter Bank Rate (TIBR) that was launched in August 2018, in what the National Bank of Georgia said was "of great importance for the development of the GEL money and capital markets" and which could be used for both cash and derivatives contracts.[30]

With similar support from the EBRD, Turkey introduced the Turkish Lira Overnight Reference Rate (TLREF) in June 2019, and Egypt launched the Cairo Overnight Interbank Average (CONIA) benchmark two months later.

Morocco and Ukraine introduced, respectively, the MONIA and UONIA benchmarks in 2020 and a reformed TONIA benchmark for the Kazakh tenge has been in place since the end of 2020.

In all markets where viable money market benchmarks have been created, the EBRD supports their usage by using the benchmarks in its own transactions, be they loans, derivatives or bonds.

---

30 The National Bank of Georgia website: www.nbg.gov.ge

5. Capital Markets and Support for a Post-Covid Recovery

In June 2020, Ukrainian economist Alexander Pivovarsky took over the LC2 team from Küüsvek and, after a review of responsibilities relating to its activities across the wider Bank, the group was renamed Capital Markets Development (CMD).

Pivovarsky stressed that the EBRD's capital market objectives remained unchanged and that the team's support for policy reform and product development would continue. It was, he said, important to ensure that progress in capital markets development be appropriately recognised in the operational assessments of transition and that activities were further mainstreamed across the Bank.

Looking to the future, Pivovarsky pointed to the very strong emphasis on data gathering and analysis and the ability to assess market development.[31]

Similar to the money market diagnostic frameworks established in a number of countries, the Treasury, CMD and other groups were working on a financial markets development index. Although still embryonic, the envisaged index would provide a systematic assessment of capital market development across a series of pillars—including macroeconomic policies and stability, the legal and regulatory environment, and market structure and access.

Pivovarsky said the index would help determine what was really a priority for any country, with dialogue based around facts rather than hopes. With the backing of the index, it would be easier to articulate what the operational teams were doing and why.

At the start of 2021, it was becoming increasingly clear that the mobilisation of alternative sources of financing through capital markets would be needed to support post-Covid 19 recovery in the EBRD's countries of operations. Funding needs were expected to be above the capacity of the banking system to deliver, making the ability to attract private capital key. Stronger capital markets help to increase the "shock absorption" capacity of the wider economy.

Against this backdrop, Pivovarsky considered continued EBRD support for capital market reforms was essential. The EBRD could also play a role of "honest broker" in light of a growing role of the state in the economy and increased demands on national authorities in response to the crisis.

31 Interview, 2021.

The EBRD's further support to create well-functioning, efficient and sustainable capital markets was expected to help financial sectors across its regions meet their post-Covid economic goals and contribute to the economic resilience of countries of operations.

II. GOOD GOVERNANCE

6. Good Governance and Economic Performance

In her foreword to the 2019 *Transition Report,* called "Better Governance, Better Economies", the EBRD's newly appointed Chief Economist, Beata Javorcik, wrote: "Good governance matters. ... There is a significant economic and social dividend to be reaped from improvements in governance at country, region and firm level."[32]

The Report emphasised the importance of strong governance as one of the six key qualities of a well-functioning economy.

Jarvorcik gave three reasons why poor governance was detrimental to performance. It creates uncertainty which is bad for business investment and causes stress to people which "discourages them from investing in their futures". Second, it damages competitiveness. Corruption imposes costs on businesses, education and access to health services from the need to pay bribes and the delays involved. The third reason was that it leads to an unlevel playing-field by conferring advantage on certain groups, to the detriment of others. Inequality of opportunity leads to an inefficient allocation of resources and disillusionment with political institutions.

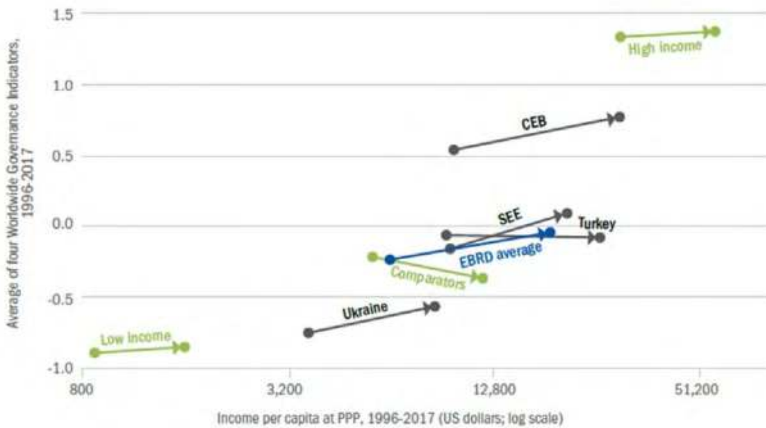
The EBRD's analysis showed that while there had been clear improvements since the 1990s in the "governance gap" of transition countries relative to advanced economies (see Figure 8.2), this had now mostly come to a halt, and in some cases showed signs of reversal.

Yet, it was estimated that:

> Closing half the gap between the quality of economic institutions in the EBRD regions and the G7 average would boost income growth per capita by an average of 0.9 percentage points a year across the EBRD regions as a whole.

32 EBRD *Transition Report 2019–20*, Foreword, pp. 8–9.

Figure 8.2 Improvements in the Quality of Governance of Institutions, 1996–2017



Source: IMF, World Bank and authors' calculations.
Note: The quality of economic institutions is captured by a simple average of the Worldwide Governance Indicators for control of corruption, the rule of law, regulatory quality and government effectiveness. "Low-income" economies are those with per capita incomes below the lowest value observed in the EBRD regions in 2017; "high-income" economies are those with per capita incomes above the highest value observed in the EBRD regions. Gross domestic product (GDP) per capita in comparator economies lies between the lowest and highest values observed in the EBRD regions. "CEB" denotes central Europe and the Baltic states; "SEE" refers to south-eastern Europe.

Source: Transition Report 2019–20, p. 15.

There were two countries in the region, Georgia and Serbia, which showed how economies that achieve particularly remarkable improvements in governance (relative to the global average) outperform their peers. Over the period 1996-2017, the report said, Georgia's improvements in governance allowed it to grow 3.5 percentage points a year faster than might have been expected, compared with economies with similar per capita incomes; in Serbia, the figure was 1.2 percentage points a year on the same basis.

There were other important findings, for example that emigration was greater and regional disparities worse when governance was poor.

In the case of Albania, the report suggested that if a "newly established confidence" could be created "that the government is fighting corruption" it would have the same impact on an individual's intention to emigrate "as a wage increase of around US$ 400 per month—roughly three-quarters of the average pay rise that can be expected after moving to the intended country of destination."[33]

---

33 EBRD *Transition Report 2019–20*, p. 31.

Or, in the case of regional disparities, raising the level of governance in Romania's worst performing region (Sud-Est) to that of its best performing region (Sud-Muntenia) "would boost regional growth by an average of 1.7 percentage points a year."[34]

Looking at firm-level corporate governance, there was significant variation among countries of operations in the quality of legislation and corporate practices, with weak non-financial disclosure and unclear responsibilities between boards and independent directors cited as particular concerns. When it came to management, foreign-owned firms tended to be better managed than domestic firms, with the gap in managerial quality particularly large in SEMED, Turkey and Central Asia.[35]

There was other evidence of corporate governance weaknesses in the EBRD regions. Most private companies were family-owned or owned by individuals, rather than under the dispersed ownership seen in more advanced countries. This was difficult to change because of weak legal protection for outside and minority investors in companies, and reluctance of firm owners to relinquish control or comply with enhanced transparency and disclosure requirements.

Studies also show that performance is enhanced by the presence of professional managers in firms. But low levels of trust and weaknesses in the rule of law and its application, for example limiting recourse against unscrupulous managers and fraudulent activities, meant only 17 per cent of family-owned firms in the EBRD regions were run by professional managers.

In most countries of operations state-owned enterprises played an important role in the economy. The quality of governance in these companies was frequently very poor. Poor governance in major utility companies, such as electricity companies, had a direct impact on the quality of infrastructure used by businesses and households and increased their costs.

There was plenty of economic evidence to suggest that independent boards and professional managers could improve state-owned companies' efficiency, and returns on equity and assets.[36] However, in several countries political interference was common owing to the absence of company

---

34 EBRD *Transition Report 2019–20*, p. 5.

35 Econometric analysis showed that only a small part of the difference could be explained by particular firm-level characteristics, such as the industry the firm operated in, size and age of firm and whether it was listed on a stock exchange. See Table 3.2, EBRD *Transition Report 2019–20*, p. 66.

36 See EBRD *Transition Report 2019–20*, p. 74.

ownership policies and the practice of making political appointments to boards and management. Board members often lacked appropriate qualifications and political goals were promoted over financial performance. State-owned enterprises often benefitted from subsidies and faced less pressures over poor service than their counterparts elsewhere and regulators were rarely truly independent.

If the transition to a well-functioning economy was to succeed, it was clear that attention had to be paid to improving governance and institutional quality in many countries of operations.

For Milica Delević, a former Serbian Assistant Foreign Minister and today Head of the EBRD's Governance and Political Affairs team:

> The quality of governance influences the level of economic development and whether it's attainable. The EBRD has developed specific expertise and a comparative advantage in really knowing the private sector and understanding what it needs in terms of effective economic governance. We know how to engage with both companies and governments, and how to support dialogue between them, and this can help effect business-supportive policy changes and improvements in governance.[37]

A wide acceptance by both government and businesses of the need for better institutions and good governance to support economic growth and transition gave prominence to EBRD efforts in this field. Some areas of EBRD activity supported improvements in the business environment through tackling governance issues at a national or regional level, for example by developing platforms for public-private dialogue to identify and address constraints to the business environment, supporting business recourse mechanisms such as business ombudsmen to give confidence to investors and supplying advice on better regulation and legislative amendments to strengthen the investment climate. Other contributions operated at the enterprise level to raise standards and quality of corporate governance.

37 Interview, 2021

7. Governance at the National Level

For many years, the EBRD as a transaction-led bank had looked into the integrity of prospective clients as it decided whether to provide companies with investment finance. As this work evolved a separate department, the Office of the Chief Compliance Officer (OCCO), was created to support the due diligence process and was staffed with specialist investigators.

Separate work on legal transition and corporate governance matters also helped to address the wider impact of corruption and other impediments to a permissive business environment. But there was less focus and engagement at a national policy level.

According to Delević, a more targeted approach towards national policy efforts to tackle anti-corruption and strengthen investment climates took off after the *Transition Report 2013*: 'Stuck in Transition' and was helped by the development of the 'well-governed' transition quality:

> The introduction of the well-governed transition quality allowed the Bank to engage more and have a more analytic and systematic framework for looking at standalone policy interventions at the national level. As a project-lender we hadn't focused very much on what needed to be done at national policy level. With 'Stuck in Transition' it became obvious that talk of 20 years of successful operations missed the fact that some patients had died! It's not enough to populate a bad policy landscape with good projects alone.
>
> So, to be sure that EBRD projects were not just islands of positive deviation but promoted change to the fullest we wanted to make sure they did so in the best possible environment. Sometimes you need to make interventions at the national level to make the business environment more enabling.[38]

In the aftermath of the global financial crisis there had been a noticeable loss of momentum in progress to strengthen the application of the rule of law, control of corruption and wider reforms to improve government effectiveness. After a period of post-crisis reflection (see Chapter 2), Management and Board Directors were more conscious than ever of the importance of

38 Interview, 2021.

good governance and institutional improvements. Officials were concerned that further weaknesses in these areas would adversely affect investor perceptions and damage long-run growth.

Anti-corruption and good governance were also matters that the EBRD President cared about strongly. Chakrabarti was keen for the Bank, with its unique mandate, to make a difference here as far as it could and he made a point of raising corruption and governance issues with presidents and prime ministers as he toured the EBRD regions after taking office in 2012.

The Investment Climate and Governance Initiative (ICGI)

As a response to the analysis in the *Transition Report 2013*: 'Stuck in Transition' and to questions from the Board on how the Bank intended to respond to its findings, the economists and political counsellors, then still in OCE, along with their legal and compliance counterparts began to develop some overarching ideas to address the governance issue. They were encouraged to do so by the President's Office.

What was needed was an umbrella approach that brought together the existing useful but limited governance projects in one place and a mechanism to drive them forward in a more coherent fashion. The goal was to improve governance in the round—economic, political, legal and corporate—through policy reform engagement, but to do so as a complement to the investment purposes of the Bank, that is from the perspective of facilitating private sector development and market efficiency.

These ideas were brought together in an Investment Climate and Governance Initiative (ICGI). This was not launched with the same fanfare as other Bank initiatives, but first appeared at an Information Session for the Board in January 2014.

Early preparations on how the ICGI might be implemented had been underway, in Albania for example. But with the Revolution of Dignity happening on the streets of Kyiv as the depths of the 2013-14 winter approached, a sense of urgency was given to the task.

The bloodshed that ensued in Ukraine just weeks after the Information Session gave even more prominence to the need for a coherent EBRD response to national and regional governance issues.

The ICGI was built around four themes: strengthening public-private dialogue, mainly through focused Investment Councils; providing recourse

mechanisms for businesses with legitimate complaints over the infringement of their rights by state entities; building capacity in state institutions responsible for economic governance;[39] and enhancing transparency in business reporting and streamlining business regulation.

To make the Initiative more credible it was important to show that there was a serious commitment by each Government involved in it to discussing and implementing better practices across a number of areas. This was to be managed by negotiating in each country a Memorandum of Understanding (MoU) between the government, independent business representatives and international institutions.

A first MoU, the Albanian "Cooperation in support of the Investment Climate and Good Governance", was signed by Chakrabarti and Prime Minister Rama on 4 February 2014. Its main focus was on establishing a high-level Investment Council to facilitate dialogue between the government and private sector.

A second agreement, with Ukraine, followed soon afterwards. "The Memorandum of Understanding for the Ukrainian Anti-Corruption Initiative" was established between the Ukrainian government, five business associations, the OECD and the EBRD on 12 May 2014. This aimed to deal with corruption and unfair treatment of business and proposed the creation of an independent "Business Ombudsman Institution".

The development of the Ukrainian MoU was made easier by the fact that the EBRD had already been working with officials to address governance issues, especially Ukraine's endemic corruption, before Yanukovych and his regime were ousted in February that year. As described in Chapter 5, progress to that point had been mired in procrastination and delay, including Yanukovych's refusal to sign any anti-corruption agreement. It was the Revolution of Dignity, and civil society's demand for improvements, that opened the door to change.

The earlier preparations meant that the EBRD, and others involved like the OECD, were familiar enough with the problems and legislative requirements to be able to translate ideas into actions swiftly. A new and willing Ukrainian government ensured rapid agreement.

Later in the year the MoUs were also signed with Moldova and Serbia.

---

39 As an example of this, see the section on the Ukraine Reform Architecture in Chapter 5.

Investment Councils

The idea of bringing together the business community and government leaders in countries of operations through Investment Councils (ICs) had been pursued by the EBRD from 2007 as a feature of the ETC Initiative.[40] They were mostly devices designed for relationship management purposes, with their main starting point the facilitation of dialogue between the government and private sector where previously there was none.

In Tajikistan,[41] for example, the Investment Council aimed to create opportunities for constructive engagement between the authorities and business, particularly for small and medium-sized businesses where access to decision-makers was very limited. Chaired by the Tajik President, it is still providing access to the highest levels.

The early ICs had some success in bringing a higher profile to the difficulties experienced by many smaller businesses from harassment by government entities and officials. The EBRD's involvement provided a level of trust that was frequently absent between government and business in these countries.

When the ICGI took off in 2014, however, efforts were made to make ICs more structured and their number expanded to include Albania, Georgia and Moldova, and later Belarus and Uzbekistan. As one pillar of the ICGI they were reflected in the MoUs agreed between the EBRD and host Governments.

The ICs provided a means for the private sector to have a greater input in decisions that affected them and to be able to share their experiences with policymakers, who generally understood less well the market implications of policy changes, and to help design and prioritise reforms. Operating as open, transparent institutions they could improve the effectiveness of governance and the momentum and monitoring of reforms.

Chakrabarti outlined his vision of the ICs' work:

> Public-private dialogue can take various forms. However, in order to have systemic impact, such dialogue needs an established, trusted platform. That platform should be a forum for regular meetings between the

40 A Foreign Investors' Council was established in Kazakhstan with the EBRD's help a decade earlier.
41 ICs were also established at that time in Armenia and Kyrgyz Republic, Mongolia, and Ukraine.

> authorities and the business community, one at which businesses can air their concerns and the government can respond in a credible way.[42]

The platforms for dialogue between the public and private sectors that the ICs offered were normally attended by high-level representatives of government, and in almost all cases were chaired by the prime minister or president of a country. Trust and credibility were enhanced by the presence of representatives from the international community, including the EBRD.

The Bank funded IC secretariats with the help of the SSF and donor funds, notably from Italy's Central European Initiative and the UK's Good Governance Fund.[43] The secretariat would organise structured agendas based on what businesses and investors were finding troublesome for their ability to operate effectively.

It was important that the secretariat, especially its head, was seen as competent and independent by both main parties. They needed to show a sound understanding of their role to ensure a good dialogue and regular, well-attended meetings. A charter, setting out the objectives of the IC, how it would operate and clear and transparent rules of membership, was also important to success.

Hester Coutanche, a senior governance adviser, believes ICs were useful since they provided "a means for discussing potential opportunities to help address the constraints facing businesses". Especially for less well-connected companies, "it was an important platform to have an open and transparent dialogue around the key issues that needed to be dealt with as part of the overall reform approach in the country."

It was when governments showed an appetite for reform, and a willingness to change policies, that these public-private platforms had their greatest value, Coutanche argued: "Support from the Government is absolutely key to having an Investment Council that works. The success of an IC is down to the will of the Government to make it happen and have a genuine desire to listen and respond to the private sector."[44]

---

42 Axel Reiserer, 'Investment Councils make a difference', 3 March 2017, https://www.ebrd.com/news/2017/investment-councils-make-a-difference.html.

43 In 2015, the UK Government and the EBRD established an EBRD-UK IC and Governance Fund with a budget of £2.6 million. Funds from the SSF were also used.

44 Interview, 2020.

Some ICs focused on domestic issues, as in Armenia where the problems of SMEs were the main concern, while in others, Uzbekistan for example, the agenda looked at ways to build the confidence of foreign investors to come into the market. In Georgia, both dimensions featured.

Coutanche explains that for many of these less advanced transition countries: "The fact that the ICs are recognised and valued by both governments and private sectors means they are having an impact by building trust."

Delević points to Albania and Georgia as particularly successful cases.

Albania was a country that emerged only slowly from a long period of isolation and confidence in public institutions was especially low. Family and close connections were the main source of trust in its largely informal economy, where illegal activities were significant. The business environment was far from propitious. In 2005, for example, Albania ranked 117th out of 155 countries in the World Bank's *Ease of Doing Business* index.[45]

A detailed analysis of the obstacles facing Albanian businesses from the fifth round of the EBRD-World Bank *Business Environment and Enterprise Performance Survey* (BEEPS V), carried out in 2012–14, found that access to electricity, competitors' practices in the informal sector and corruption were seen as the biggest obstacles to business by companies facing the most severe problems.[46,47] These difficulties were rooted in a weak investment environment and governance failures.

A new government was formed in September 2013, led by Edi Rama after eight years in opposition, which aimed to tackle these deficiencies. Following discussions between the Albanian Prime Minister and the EBRD President, a pilot MoU was signed five months later.

The Government, keen to pursue reforms that would assist Albania's EU accession process, committed under the ICGI to establish an Investment Council as a key mechanism for reform.[48] The MoU said:

---

45 *Doing Business in 2006*, World Bank/IFC, September 2005.

46 'Firm performance and obstacles to doing business in the Western Balkans: Evidence from the BEEPS', A. Krešic, J. Milatovic and P. Sanfey, EBRD Working Paper No. 200, January 2017

47 An econometric analysis in the same paper which assessed the biggest costs revealed by firms from obstacles to doing business came from taxes (tax rates and administration), access to electricity and competition from the informal sector, ibid. p.17

48 Three other commitments under the MoU were to strengthen the functioning of the judiciary, improve the business registry and help design an effective consumer credit bureau. www.ebrd.com/documents/corporate-strategy/icg-mou-albania.pdf

> The Government … intends to … promote the work of a dedicated Investment Council to support the National Economic Council … implement … measures suggested by the business community … and lead efforts to strengthen the rule of law, prevent corruption, reinforce mechanisms of dispute resolution, enhance transparency and address the issue of informality in the economy.

Meeting four to five times a year with the participation of the business community and IFIs, the Investment Council has since endorsed more than 250 reform recommendations, half of which have been implemented by relevant government institutions. Improvements have been made in areas such as dispute resolution mechanisms, measures to address the informal sector, especially in tourism and agribusiness, VAT refunds and simplification of tax and customs administration and in regulatory inspections for businesses.

An assessment by the EBRD Evaluation Department noted that:

> [The ICGI] has improved governance standards by increasing transparency and accountability … Government support was a prerequisite for the Council's success in Albania. … Initially, the level of trust in the IC was very low but it is increasing as the private sector sees that the Council's priorities and actions are led by technical experts, and not by government officials.[49]

Business Ombudsman Institution

A second major feature of the ICGI was to provide redress mechanisms for businesses facing corruption and other impediments to the smooth working of their commercial activities. A prominent and innovative example, the independent Business Ombudsman Institution (BOI), was established in Ukraine in 2015.

With the Ukraine ICGI MoU in place in 2014, which provided explicitly for the adoption of a BOI, the EBRD sent a senior governance specialist to Kyiv to lead the work that resulted in the establishment of a Business

49 'Special Study: The EBRD's Investment Climate Support Activities Albania Case Study', p. 20, EBRD Evaluation Department, February 2018.

Ombudsman Council.[50] The Bank was instrumental in putting in place the necessary institutional, legal and organisational arrangements for it to function.

Unlike a traditional business ombudsman, who is appointed and dismissed by government authorities, the BOI could only be appointed unanimously by the BOI supervisory board—comprising the government, business associations and international organisations—and could not be dismissed without a two-thirds majority vote by the same board.

The BOI was a novel independent recourse mechanism that sought to protect the basic rights of businesses and entrepreneurs and investigate claims that state authorities have abused their powers. It drew broadly on some elements of the High Level Reporting Mechanism (HLRM) principles developed jointly by the OECD, the Basel Institute of Governance and Transparency International in 2013, which in turn had been prompted by rising G20 concerns over global corruption.[51]

The EBRD and other international bodies had consistently argued that Ukraine's anti-corruption institutions needed independence and operational capacity to be effective. So, it was clear for the Business Ombudsman Council to work well it needed fairly extensive investigative powers, as well as strong legal protections against possible actions by government authorities designed to prevent it from conducting objective and rigorous investigations.

Once these governance protections were in place the BOI opened for business in May 2015. It was only the second case globally (along with Colombia), where the core principles and standards of HLRM had been applied and followed through comprehensive governance instruments.[52]

While the BOC was able to draw attention to various systemic failings and thereby improve the investment climate its recommendations were not binding. There was no intention for the Ombudsman to interfere with normal legal proceedings or court decisions. Instead, it could contribute to

50 The terms Business Ombudsman Council and Business Ombudsman Institution are used interchangeably in this context.

51 See https://www.oecd.org/corruption/High-Level-Reporting-Mechanism-Overview.pdf and the St Petersburg Strategic Framework agreed by G20 Leaders in 2013 https://www.unodc.org/documents/corruption/G20-Anti-Corruption-Resources/Principles/2013_St._Petersburg_Strategic_Framework_for_G20_ACWG.pdf.

52 'Investment Climate Support Activities, Case Study: Business Ombudsman Institution in Ukraine', p.4, EBRD Evaluation Department, July 2018.

improving the business environment by making recommendations to the Ukrainian authorities in individual cases and via reports, for example on reform of law enforcement institutions such as the Prosecutor's Office and the State Security Service, as well as by issuing regular reports on its investigations and more detailed analyses on wider systemic issues.

The EBRD shaped the structure of the BOI and provided support through the EBRD-Ukraine Stabilisation and Sustainable Growth Multi-Donor Account, which is funded by a large number of donors with more than half of the funds provided by the EU.[53]

The first Business Ombudsman in Ukraine was selected through a competitive process, with the representatives of the three main parties—government, business associations and international organisations (represented by the EBRD and OECD)—each having one vote. Algirdas Šemeta, a former Lithuanian Minister of Finance and European Commissioner, was officially appointed in December 2014.

The appointment of two deputies and a staff of investigators, by competitive selection, followed. The BOI staff reached a total of 14 full-time employees by mid-2015 and, as demand for its services grew, expanded to around 30 a few years later. In October 2019, Marcin Święcicki, a former Polish member of parliament and a mayor of Warsaw, became the second Business Ombudsman in Ukraine.

The results have been impressive. In his latest published report to the end of 2020, Święcicki notes that there have been 8,265 complaints from businesses since May 2015, with more than two-thirds "investigated in detail". "Out of all closed cases more than a half were solved successfully," he says. By the end of 2019, he claims: "We assisted in recovering almost UAH 18 billion [US$ 745 million] imposed on business unlawfully."[54]

In 2020, 74 per cent of complaints were lodged by SMEs and 87 per cent originated from Ukrainian local enterprises. The biggest number of complaints concerned tax inspections, closely followed by appeals over actions by law enforcement bodies. There were also complaints concerning failures of state bodies to carry out court decisions and over property rights protection.

53 The EU, UK, Sweden, USA, the Netherlands, Norway, Finland, Denmark, Switzerland, France, Germany, Italy, Japan and Poland.

54 Business Ombudsman Council, 2019 Annual Report, Kyiv, Ukraine, April 2020, p. 4.

The institution has been an evident success. An EBRD Evaluation Department review concluded:

> Initiating and supporting the activities of the Ukrainian BOI is one of the most successful examples of the Bank's non-investment operations in the country. … The BOI is effectively a substitute for dysfunctional dispute resolution between private businesses and state agencies. … The BOI has become a trustworthy institution in the eyes of the public. This is a great achievement since trust is something that Ukrainian state institutions have persistently lacked.[55]

Success in Ukraine gave encouragement to others to consider a similar route. A recent example has been in the Kyrgyz Republic.

In the past, persuading Kyrgyz business associations to engage in more open and collective dialogue with the authorities had been challenging for fear of clashes over their powers to defend businesses. However, when they met the Ukrainian Ombudsman, its clients and heard about the tangible results the institution was able to deliver without compromising the business associations they realised how the arrangement could help them.

Anastasia Rodina, a senior governance adviser based in the region, describes the sea-change in attitude:

> After learning about the Ukrainian Ombudsman at an OECD/EBRD event, the Kyrgyz stakeholders were invited to Ukraine to see how the BOI worked in practice. The business delegates became so convinced of the value of an Ombudsman office they decided to be the driving force behind one in Kyrgyz and formed a working group to draft decrees and establish it! It was based on the Ukrainian (EBRD) model and ensured the key principle of independence.[56]

The Kyrgyz Institute of Business Ombudsman opened for business in February 2020 with Robin Ord-Smith, a former UK Ambassador to the Kyrgyz Republic, selected by open competition as its first Ombudsman. Although 2020 was a challenging year, the Kyrgyz BOI established itself as

55 Case Study, Business Ombudsman Institution in Ukraine, p. 14.

56 Interview, 2020.

a trusted partner of businesses, saving them over US$ 1 million, and helping to voice their concerns over the pandemic challenges.

8. Legal Reforms and Better Regulation

Public rules, practices and regulations which affect the conduct of business in market democracies are underpinned by well-established legal arrangements and legislative procedures. In emerging markets, the underpinnings derived from the rule of law are often less securely based than in advanced economies. This was especially true of EBRD countries of operations as they first emerged from the world of command economies.

Despite significant improvements from those early days, weak governance surrounding public institutions and regulatory regimes has remained a problem in many countries in the EBRD regions since then.

A Legal Transition Team

From the moment the EBRD started operations in 1991 the legal department became heavily engaged in work on the Bank's investment transactions. As business volume grew so did the number of lawyers dealing with the documentation and negotiation of the Bank's loans, equity investments and other financial operations. They were also instrumental in ensuring clients' adherence to the Bank's rules and procedures, compliance with financial agreements and other legal requirements relating to Bank operations. Today more than half of the Office of the General Counsel (OGC) is made up of transaction lawyers.

Early in the Bank's life it was recognised that legal work was needed beyond the immediate transaction level in view of the rudimentary state of legal and regulatory arrangements in countries of operations at the time. Shortly after the successful publication in 1994 of a model law on secured transactions, which set standards for the design of laws on the taking of security over movables in several countries of operations, a small team was set up in 1995 by John Taylor, then General Counsel, which became the Legal Transition Team (LTT). It was developed further by his successor, Emmanuel Maurice.[57]

---

57 See Kilpatrick, *After the Berlin Wall*, Chapter 3, p. 74.

The effective application of the rule of law required not only sound legislation and regulations to be in place but also an understanding of how the relevant laws and ordinances should be implemented in particular sectors and country circumstances. Legal impediments to business sapped efficiency and innovation so improvements to the legal landscape were vital to the generation of investment opportunities and markets development more generally.

The task of LTT was to find ways to raise standards of the laws and regulations in the countries across the EBRD region necessary for their transition to fully functioning market economies, thereby facilitating the work of EBRD's bankers and transaction lawyers on investments.

The main idea behind the approach, which continues to this day according to Michel Nussbaumer, the current Director of LTT, was to create a "virtuous circle of legal reform". This took the form of introducing relevant international legal standards as a first step, creating reference norms that countries could use to build their legal regimes.

Assessments of the quality of countries' commercial legislation and practices would then be measured against these standards. As a next step, support would be given through technical assistance projects to help prepare and make amendments to legislation and regulations, along with related work to strengthen implementation and enforcement capabilities. Finally, the dissemination of information on legal practices and advances would be conducted through outreach programmes in countries of operations.

One early example of the approach which derived from the model law work was legislation on secured transactions in the Slovak Republic in 2000. Another success story was the contribution to the preparation of the Russian Corporate Governance Code in 2002.

A decade or so later, after a request from the Central Bank of Russia (CBR), the team made a significant contribution to a review and strengthening of the Code and its implementation. The new Code that followed in 2014 required listed companies to disclose their compliance with the Code and to explain the reasons for any lack of compliance. Annual monitoring reports on the implementation of the Code were published by the CBR as part of the new arrangements, helping companies realise disclosure was being monitored and become more aware of the importance of what they published in their annual reports.

A further example from the mid-2000s involved the team branching out to increase judicial capacity in the commercial law sector in the Kyrgyz

Republic. This was done in collaboration with the International Development Law Organisation (IDLO), an intergovernmental organisation promoting the rule of law and related training.

As experience grew, the Bank aimed for standards first suited to local capacity, usually by working with local counsel alongside relevant officials, to introduce progressive steps towards international best practices. New laws and regulations were thereby introduced which were better suited to existing systems and easier to implement and enforce. As a result, the process of reform suffered from fewer setbacks and was better appreciated by local stakeholders than efforts to apply international standards in one fell swoop. The results were also more long-lasting.

The approach was effective in opening up investment opportunities. Legal advice was given in a wide range of areas designed to support the development of a predictable investment climate where it was most relevant to the Bank's investment activities. Among these areas was work on PPPs and concessions to facilitate infrastructure investments, changes in laws that related to access to finance, insolvency and debt restructuring, efforts to improve dispute resolution through improvements in the judicial sector and through mediation activities, more transparent public procurement and legislation to promote resource efficiency.

There were a host of more specific areas where the legal transition team's expertise could be applied, including improving credit information reporting systems, assisting with commercial law to judicial training in competition law and capacity building of competition authorities. Efforts were also made to strengthen regulation in competitive sectors such as telecommunications and banking.

Georgia's PPP legal and policy framework

Growing demand for public infrastructure created demand for private sector participation, especially in countries facing fiscal constraints. Weak state capacity in managing large infrastructure projects and in meeting demanding technical standards strengthened the case for private sector involvement.

However, the legal and economic framework had to be adequate to attract high-quality private sector infrastructure companies. LTT was able to help prepare clearer rules governing concessions and more transparent laws on

PPPs in several countries which matched investors' needs and attracted private sector support.

In Georgia, for example, work with the legal authorities began in 2015 on developing a PPP law that could support private sector investment and modernise the economy. By May 2018, the Parliament had adopted the PPP law and corresponding amendments to other primary laws enabling its practical application. PPP secondary legislation prepared by the Asian Development Bank (ADB) with the EBRD's help was issued in summer 2018.

The new PPP law provided clear guidance on definitions, project identification, initiation and preparation, as well as detailed procedures for the selection of private partners. It also marked out the stages of project implementation and post-implementation relationships. The work ensured all the elements for a comprehensive and effective legal framework were in place to promote investment in Georgia's infrastructure and improve public services.

Expanding the legal transition programme

Two factors helped LTT's work—the Bank's Legal Transition Programme (LTP)—expand more quickly in the 2010s.

The first related to the Shareholder Special Fund (SSF), derived from allocations of the Bank's net income, which had been created towards the end of the previous decade. This provided greater access to the technical assistance funds that were essential to the programme. Bilateral donor funds, such as those made available by Japan, Switzerland, Taipei China and the UK, and later Luxembourg and South Korea, also helped.

As compared with bilateral funds, the SSF had the advantage of speed, since no lengthy negotiations with donors were needed. It also helped LTT maintain more consistent relationships with recipient governments, since there were fewer gaps in funding availability, such as when donor funding had to be renewed with existing donors or past donors had to be replaced by new donors. The conditionality attaching to the use of SSF funds was also more consistent and less burdensome than with bilateral donor funds. Since 2016, the majority of LTP funding has been from the SSF.

The second factor was the greater prominence to the work of the team that came in the wake of the global financial crisis. The recognition of the importance of strong institutions in fostering the transition strengthened

the demand for the team's services. It became more visible across the Bank as a useful source of expertise which could help improve the environment for business in countries of operations. Chakrabarti's message on the importance of policy engagement and structural reform was a further spur to these law reform activities. And the clearer strategic focus of country strategies, including with the introduction of Priority Policy Objectives (PPOs) in strategies, also supported this work.

As a result, both the number and value of projects managed by the team rose threefold in the 2010s, compared with the previous decade, and the team grew to around 20 people dealing with around 80–90 projects per year. The advent of the transition qualities showed projects were most commonly designed to improve governance (under "well-governed"), but not exclusively, with several projects strengthening the resilience quality, as for example through work on non-performing loan (NPL) regimes, and competitive performance. The LTP was also a strong contributor to the PPOs, where the team led, individually or jointly, up to 20 PPOs a year, or around 15–20 per cent of the Bank's total.

The legal reform needs of early transition countries were the biggest drivers of the work though some technical assistance was also given to EU member states (via EU funds). Recent examples show how digital transition and related innovations in policy may reverse the typical direction of policy impact, whereby Poland and Greece have expressed interest in open digitalisation of public procurement after seeing its successful implementation with the EBRD's help in Moldova and Ukraine.

The Ukraine case on public procurement demonstrates how the work of the legal transition programme improved governance at the national level and led to better practices that enabled businesses to gain access to contracts in a fairer and more competitive manner.

ProZorro, Ukraine

Many private companies in western economies look to public procurement of goods and services as an important source of business, and private sector expertise properly applied improves the efficiency of public services. In some areas, state procurement can help the private sector develop innovative technologies. However, in emerging markets the odds are often stacked against the majority of private firms from fulfilling these roles when the politicians

in charge of public procurement use contracts as a means to win or repay favours among a close circle of business supporters.

In Ukraine, with an annual public procurement budget of some US$ 20 billion, misuse of public procurement was no exception. Decades of concealment and corruption allowed the country's ruling elite to exploit the state procurement system in their interests.

The huge gaps in the Ukrainian public procurement system were more readily addressed in the new, more receptive environment after the Revolution of Dignity. The Bank's legal transition team was able to promote modern regulatory policy and contribute to the approval of a new procurement law in 2015.

This law complied with the World Trade Organization's (WTO) Agreement on Government Procurement (GPA) standards and requirements. The EBRD worked with the Ukrainian government to complete the GPA negotiation process in September that year.

The adoption of WTO public procurement policy standards held several advantages for Ukraine. The GPA introduced good governance standards and stimulated competition and growth by allowing businesses from other GPA countries to bid for Ukrainian public contracts. Under GPA market access, international suppliers from more than 48 countries would participate in public tenders in Ukraine. At the same time, becoming a GPA member increased the size of the public procurement market available to Ukrainian businesses globally.

As the negotiations on Ukraine's WTO GPA accession progressed, the focus of EBRD support shifted towards meeting GPA transparency standards in practice. This involved developing an independent complaints mechanism and a national-level electronic procurement system for state purchasing of goods, works and services.

Building on the innovative ideas of the civic activists who had sought increased transparency and reduced corruption after the 2014 Maidan protests, the Bank supported a coalition of Ukrainian civil society organisations (led by Transparency International Ukraine), businesses and government officials in developing a pilot concept in early 2015 called "ProZorro", a new model of e-procurement based on the Open Contracting Data Standard (OCDS).[58]

58 Transparency International was initially guardian of the "electronic" keys to the ProZorro platform (so that

Prozorro means transparent in Ukrainian, reflecting the aim of full transparency of public procurement decisions by making procurement information open to all online. This was achieved by making the ProZorro system connect a new open source central database to existing platforms, and made full proactive disclosure of procurement data available in real-time.

By making procurement information open to anyone, corruption risks were reduced while real-time access improved economic efficiency. Procurement officers across Ukraine could access information on suppliers and contracts for example, or publish new online tenders in a few minutes, something which would take days in many richer countries.

The ProZorro pilot was very successful, attracting almost 1,000 contracting entities within first three months of its operation. Local suppliers began to trust the public procurement market for the first time, helping to strengthen competition and deliver better value for money for Ukrainian taxpayers.

The ProZorro system became mandatory from 1 April 2016 for all public institutions, local governments, state-owned enterprises in small or large-scale purchases and has developed into one of the most advanced e-procurement platforms in the world.

ProZorro won several international awards[59] for transparency safeguards and digital innovation and publishes annually about four million electronic tenders from about 41,000 public buyers in Ukraine.

Ukraine's Ministry of Economic Development estimates that between 2015 and 2020 ProZorro saved as much as US$ 4.1 billion of public funds.

Other results are also impressive. In 2020, the number of registered domestic and international suppliers reached 260,000 while the share of procured value through competitive procedures increased from 25 per cent before the launch of ProZorro to 76 per cent. New bidders reached a total of 71,000 in 2020 and the number of online platforms participating in ProZorro went from zero to 38. Ukraine's ranking in the UN e-participation index moved up considerably, to 46th out of 193 countries by 2020 from 83rd

the Government was not able to interfere with the system). The system was fully transferred by TI Ukraine to the government (Ministry of Economic Development and Trade) when made mandatory by law on 1 April 2016.

59 The 2016 World Procurement Award, the 2016 and 2017 Davos Awards, and the 2016 Open Government Award.

in 2012.[60] An econometric analysis of the effects of ProZorro, published in 2019 by the Center for Global Development, found:

> There is evidence of a greater number of bids, higher savings, and greater participation in provision of contracted goods and services (more unique winners per tender in each entity), as well as strong evidence of reduced time to procure goods and services.[61]

Civil society organisations and others across Ukraine became familiar with the public procurement system and could report tender violations and other risks, supporting independent monitoring and an improved culture in public procurement. A survey of companies by Transparency International Ukraine in 2019 showed 80 per cent of respondents were satisfied with work on the platform, and 41 per cent of users said they had never encountered corruption in ProZorro.

The Open Government principles have been applied elsewhere. A similar online platform, ProZorro.Sale, was launched in 2017 for selling Ukrainian state and communal property and assets, including NPLs, mineral extraction rights, rail car leases and more. According to estimates,[62] between 2017 and 2019 ProZorro.Sale delivered income of UAH 21 billion (US$ 840 million) through 241,000 auctions on 50 market places, including substantial sales of assets of bankrupt banks and some revenue from small scale privatisations.[63]

Following the success in Ukraine, the EBRD deployed the ProZorro Open Government concept as an e-procurement standard in a number of other countries, including Moldova, the Kyrgyz Republic, Tunisia, and Uzbekistan.

---

60 The index looks at the use of online services to facilitate provision of information by governments to citizens (“e-information sharing”), interaction with stakeholders (“e-consultation”) and engagement in decision-making processes (“e-decision-making”). https://publicadministration.un.org/egovkb/en-us/Data/Country-Information/id/180-Ukraine/dataYear/.

61 A. Kovalchuk, C. Kenny, and M. Snyder, ‘Examining the Impact of E-Procurement in Ukraine’, Center for Global Development Working Paper 511, June 2019, https://www.cgdev.org/publication/examining-impact-e-procurement-ukraine.

62 ‘Deep Dive Case: Public Procurement Case’, p. 54, Annex 8 in ‘Legal Transition Programme – Annexes’, EBRD Evaluation Department, 2020.

63 See I. Lakhtionov, ‘From Startup to Reform. ProZorro.Sale is transferred to the Government’, *Transparency International Ukraine*, 21 February 2019 https://ti-ukraine.org/en/blogs/from-startup-to-reform-prozorro-sale-is-transferred-to-the-government/

Insolvency and debt restructuring

An important part of the financial process in a well-functioning economy is its ability to wind up poorly performing businesses and redistribute remaining assets of value. This forms part of the reallocation of resources that efficient markets facilitate. In turn, this process depends on an effective insolvency and debt restructuring regime.

The EBRD played an important role in raising standards of insolvency and debt restructuring and their application in many countries of operations. From 2005 the legal transition team began to apply 10 core principles, later increased to 15, to insolvency law regimes when making their assessments.[64]

The principles complemented two international standards: the United Nations Commission on International Trade Law (UNCITRAL) Legislative Guide on Insolvency Law[65] and the World Bank's Principles for Effective Insolvency and Creditor/Debtor Regimes.[66] The two sets of rules were brought together to create the Insolvency and Creditor Rights (ICR) Standard in 2011, recognised by the Financial Stability Board (FSB) as one of the key standards for sound financial systems.[67] The EBRD approach was consistent with this standard but extended insolvency law and practice, especially to support early restructuring.[68]

In many countries facing insolvency challenges, the EBRD was able to act quickly with its expert team, making use of well-qualified consultants and suitable local counterparts. It applied the core principles to deliver projects and conduct policy discussions with the key decision makers. In its efforts to improve insolvency and debt restructuring frameworks, the Bank operated alongside other key international stakeholders, especially the IMF, World Bank and European Commission, which helped to keep the pressure up for reform.

---

64 For the latest edition, see 'EBRD Core Principles of an Effective Insolvency System', September 2020.

65 United Nations Commission on International Trade Law.

66 http://documents1.worldbank.org/curated/en/518861467086038847/pdf/106399-WP-REVISED-PUBLIC-ICR-Principle-Final-Hyperlinks-revised-Latest.pdf.

67 https://www.fsb.org/2011/01/cos_051201/. The FSB is an international body that promotes international financial stability by coordinating national financial authorities and international standard-setting bodies to develop sound financial regulatory and supervisory policies.

68 The ICR standard, for example, also covers effective credit access and protection mechanisms, commercial enforcement and credit risk management frameworks.

The EBRD's presence on the ground helped with the frequent delays that came with enacting new laws and implementing higher standards. Its corporate recovery team was also able to assist based on its experience in dealing with impaired loans on the Bank's books which helped to reveal weaknesses in insolvency and debt restructuring regimes for future improvement.

Non-performing loans on the books of financial institutions became a very significant problem in many countries of operations after the global financial crises of the early 2010s.

It was important that resolution of bank NPLs was managed in a way that preserved overall financial stability. The legal transition team worked with national authorities to develop strategies for the resolution of NPLs and removal of impediments in legal and regulatory frameworks. Among the actions that followed were the transfer of impaired loans to "bad" (resolution) banks and the use of specialised asset management companies for enforcement and partial recovery. These efforts were conducted under the auspices of the Vienna Initiative,[69] and assisted debt resolution efforts especially in the EU neighbourhood.

Commenting on the results of 19 legal transition projects from 2011 to 2018 on insolvency and debt restructuring, the Bank's Evaluation Department said:

> The quality and speed of insolvency resolution has improved, which enhances trust in the system among market operators and prompts behavioural changes in the rule of law (Bulgaria, Croatia, Cyprus, Greece, Serbia, Kosovo, North Macedonia, Tunisia).
>
> New institutional capabilities for voluntary, mediation-based, out-of-court, financial restructuring procedures are used more widely for NPL resolution, reducing the burden on courts. This contributes to higher standards of corporate governance in banks and companies …
>
> Interventions in 14 countries over a substantial period of time have resulted in the adoption of important legislation and regulations, as well as institutional changes that enable quicker and higher quality procedures. The high quality of expertise, flexibility, and mostly timely interventions are praised by local stakeholders … Gradually enhancing the skills and knowledge of judges and legal professionals in the areas of insolvency, restructuring

69 See Chapter 2.

> and accounting, as well as strengthening the legal framework and implementation practices … improves understanding and prevents … default bankruptcy procedures [and] reduces pressure on the court system.[70]

A distinctive asset of the EBRD

For Nussbaumer, a distinct legal team focused on improvements to the underlying investment climate of countries of operations distinguishes the EBRD from most other MDBs. The build-up of its expertise since 1995 and strong engagement with the policy work of the Bank has helped with its credibility internally and externally. "Creating a distinct unit was certainly part of the success story", says Nussbaumer.

The Evaluation Department concurs. In 2021, it praised the legal transition programme highly, saying that it is "the Bank's single largest, highest profile, and probably most important advisory operation." Active in every country of operations and in most sectors it "is highly appreciated by external clients". It concluded:

> The LTP has become a distinctive institutional asset for EBRD in its efforts to improve investment climate in the countries of operation. It is a key part of EBRD's unique institutional "offer" and a key differentiator versus other IFIs and private sector financiers.[71]

9. Corporate Governance

The "well-governed" transition quality encompasses corporate-level governance, the system of rules and practices by which companies are directed and controlled. Part of LTT focused on this aspect of good governance. Like the rest of the team its work began to flourish from the mid-2000s onwards, accelerating after the global financial crisis with a stronger realisation of the importance good governance at the company level to wider institutional development and economic performance.

---

70 'Deep Dive Case: Insolvency and Debt Restructuring', p. 32, p. 36, Annex 7 in 'Legal Transition Programme – Annexes', EBRD Evaluation Department, 2020.

71 'Legal Transition Programme', p. iv, Special Study, Evaluation Department, October 2020.

Corporate governance and investment projects: SUAL and Rusal, Russia

One of the early episodes that involved the legal corporate governance team in a prominent way was an aluminium project in Russia.

In 2004, a proposed bauxite mining project, 250 kilometres south of the Arctic Circle in the Komi region of Russia, raised eyebrows among Board Directors. Bauxite is the essential ingredient in the production of alumina, the raw material used in aluminium smelting. Aluminium production was a sensitive issue when it came to Russian business.

The mining company involved was majority owned by SUAL, one of the world's largest aluminium producers which in turn was owned through the investment vehicles of two Russian oligarchs, Viktor Vekselberg and Leonard Blavatnik.

The aluminium industry in Russia had a poor governance record. In making the case for the investment, which was to be financed in parallel with the IFC, the EBRD banking team with the help of LTT lawyers presented a series of actions to be implemented by SUAL as part of the deal that would improve the transparency and corporate governance of the company. This would potentially also assist with a future public listing that its owners were considering.

Despite some misgivings the Board agreed to go forward with the operation. A year later, SUAL formed a 50/50 joint venture with Rusal, a competitor and the largest aluminium company in Russia. Directors' eyebrows rose further since Rusal was owned by Oleg Deripaska, an oligarch who had emerged a winner from the Russian 'aluminium wars' in 1990s, which had raised significant integrity issues.

In the ensuing renegotiation of the financing, the EBRD and IFC lawyers worked hard to force greater disclosure as a condition of providing the earlier promised finance. After an extensive review of Rusal's record and ownership structure, and after much debate internally, the EBRD and IFC said in January 2006 that they now planned to disburse the US$ 150 million financing (US$ 75 million each) for the Komi aluminium project.

A joint statement explained the basis for the decision was that agreement had been obtained to the full disclosure of Rusal's and Basic Element's ownership by Deripaska (Basic Element was Deripaska's investment vehicle) and commitments to transparency and good corporate governance, which would now also cover Rusal and Basic Element. Compliance with these

commitments was covenanted in the legal agreements. The statement made clear the commitments to be undertaken:

> IFC and the EBRD welcome the adoption by RUSAL of an action plan over an 18-month timetable covering significant corporate ownership disclosure, the publication of financial information and specific steps aimed at improving corporate governance—notably the election of three independent directors.
>
> These independent directors, to be appointed in agreement with IFC and the EBRD, will chair and constitute the majority of the sub-committees that will oversee audit and corporate governance as well as other corporate matters. [72]

The transaction marked the start of a greater integration of legal advice on corporate governance issues and Banking operations. Up until that point, the expertise of the small legal corporate governance team had been somewhat tangential to the core business activities of the Bank.

Gian Piero Cigna, Head of Corporate Governance in OGC, observes:

> Until that moment, the corporate governance work of LTT had little direct exposure to our investments. No-one on the Banking side was asking us for help. I was thinking "How can we develop effective legal reform without knowing the challenges that companies face in countries?" By engaging with Banking, we learnt more about the corporate governance challenges our investee companies faced and, in turn, we could translate this knowledge into better legal reform and targeted actions for these companies.
>
> The Rusal transaction was a good example of how we could make a difference. After a few months, the whole corporate structure of Rusal and Basic Element was put on the internet as a result of our work. It was the first time ever that such a level of transparency was reached in Russia.[73]

72 'IFC and EBRD welcome commitment to high governance and business standards by RUSAL Chairman Oleg Deripaska: Banks confirm financial support for Komi Aluminium project after change in ownership', IFC/EBRD, Washington/Moscow, 17 January 2006. See also 'Oleg Deripaska Brings His Core Assets into the Open', Vedomosti, Moscow, 4 April 2006.

73 Interview, 2021.

Mechanisms to deliver better corporate governance by DFIs

The relationship established with the IFC developed further. Early in 2006, the EBRD and IFC began working with the Dutch development bank, FMO, and a few others[74] to prepare a common approach to linking corporate governance improvements more directly with investment operations.[75]

President Jean Lemierre signed the EBRD up to the initiative, called 'A Corporate Governance Approach Statement by DFIs', at the Annual Meetings of the IMF and World Bank Group in 2007. It was signed by 31 DFIs.[76]

A working group, including the EBRD, followed and developed a set of tools (including a questionnaire for clients, instruction sheets, a list of corporate governance terms and sample cases) to provide a common methodology on the assessment of corporate governance in investment operations. The DFI Toolkit on Corporate Governance was launched in 2010.

The Approach Statement and Toolkit were brought together under a Corporate Governance Development Framework a year later as a common platform for evaluating and improving governance practices in investee companies. It was endorsed by 30 DFIs[77] in September 2011, once again at the Annual Meetings of the IMF and World Bank Group.

For Cigna, the introduction of the Toolkit as a "win-win". In particular, he said "it helped us plug our expertise into Banking and bankers could enhance their projects".

A key aspect of the framework was the commitment by each institution to operationalise the OECD Principles of Corporate Governance, which had been introduced some years earlier, turning principles that resonated with policymakers into a more practical approach that could be applied to individual companies.

---

74 The ADB, the Black Sea Trade and Development Bank (BSTDB) and the Development Bank for Latin America (CAF).

75 See G. P. Cigna and P. Djuric 'Improving Corporate Governance of Investee Companies – a Common Goal of Development Finance Institutions', Law in Transition Journal, 2019.

76 See 'A Corporate Governance Approach Statement by Development Finance Institutions', 19 October 2007, by IFC and other DFIs, https://www.ifc.org/wps/wcm/connect/topics_ext_content/ifc_external_corporate_site/ifc+cg/cg+development+framework/a+corporate+governance+approach+statement+by+development+finance+institutions

77 It has since expanded to 35 DFIs.

It would turn out that use of the Toolkit revealed many less obvious issues that blocked progress on corporate governance than could be seen purely from the perspective of the OECD Principles.

The rationale of the Toolkit is based on the need of a "diagnosis" before jumping to "solutions". The Toolkit assists in evaluating the practices in place at the companies under a very wide perspective: all pieces of the puzzle are looked at and put together to see what features come out. If a piece is misplaced, it is fixed.

Of course, most corporate practices depend on the legislation in place, and the LTT started mapping the good and bad practices for each jurisdiction. In 2013, the team began working on a comprehensive assessment of the legislation and practices in all countries.[78] With this renewed source of expertise, it was much easier and effective to engage with governments for the promotion of reform. The team was able to meet authorities and discuss reform avenues by clearly pointing out the aspects that needed to be tackled.

EBRD Corporate Governance Reviews

The Toolkit was adapted for internal use by introducing a Corporate Governance Review process, which was incorporated in the EBRD Operations Manual in 2014. This embedded the idea of conducting assessments of client corporate governance practices against good standards and the development of Corporate Governance Action Plans (CGAPs). The Review combined the diagnostic process of the Toolkit with a series of recommendations based on the analysis.

Because every investee company was different and required its own individual investigation of its core governance features, the team developed different methodologies for different types of companies (family businesses, listed companies, banks), which have different corporate governance challenges. Bankers in turn were able to draw on a more tailored system based on an initial screening tool which catered for six different versions of the client questionnaire. These varied according to the type of company and governance structure involved, differentiating for example between listed, non-listed private companies and state-owned enterprises.

---

78 The EBRD corporate governance assessment, which is updated regularly, is available at: https://www.ebrd.com/what-we-do/sectors/legal-reform/corporate-governance/sector-assessment.html

A corporate governance matrix, covering practices in five areas—commitment to good corporate governance, the structure and functioning of the Board, the control environment and processes, transparency and disclosure and rights of minority shareholders—measured performance against four levels of achievement, from basic corporate governance practices the EBRD expected from all investee companies to more advanced practices which investee companies should gradually aim to reach.

CGAPs soon became a regular feature of the team's work, often prompted by economist reviews of bankers' projects where there appeared to be good potential transition impact from improving the governance of a project company, especially in cases where the legislation revealed room for improvement.

State-owned enterprises

Many of the most important, and most difficult, cases concerned state-owned enterprises (SoEs). Even today, these enterprises comprise about one-half of the team's annual caseload of 50–60 projects.

SoEs tend to be in heavily regulated enterprises, such as energy utilities and infrastructure companies, or firms in strategic sectors, such as petrochemicals or metallurgy. They generally needed substantial finance, which made them attractive to bankers looking for large-scale deals. But the opportunity to extend larger amounts of finance also had some advantage in providing greater leverage for reform.

SoEs differed from private sector firms in two main ways. First, the key decisions were generally not made by the SoE itself but from outside the company by government ministers and officials. In most cases, the SoE's management would simply follow orders from that quarter.

The second difference comes from the role of regulation. These firms were mostly in highly regulated sectors so efforts to improve governance through CGAPs at the company level could not gain full traction without parallel reforms at the sector level. This meant actions were also needed to improve regulatory practices and other aspects like tariff setting.

Solutions towards good governance in SoEs thus needed a dual track approach: improvements to corporate governance within the company, but also to government practices and regulations that determined what it was able to do. Achieving clarity on roles and responsibilities in these cases was

paramount. Legal advice was required on both dimensions which the LTT was able to supply.

An important example of what was required came with a major transaction with Naftogaz in 2014 which launched a series of reforms in the company and the Ukrainian gas sector as a whole.

Improving corporate governance at Naftogaz[79]

In October 2014, the first elections since the Revolution of Dignity left the new reformist government confronting the huge range of issues needing to be solved to bring improvements to the people of Ukraine. Among the most difficult was one that had plagued Ukraine for years: delivering energy security and reform of the gas sector.

This could not be done without reform to the oil and gas group Naftogaz. The company employed more than 75,000 people and dominated the gas sector. It was responsible for around 80 per cent of gas production, three-quarters of gas imports and 70 per cent of Ukrainian gas trading.

That year losses at Naftogaz were heading for US$ 3.6 billion, amounting to 5.7 per cent of GDP, a clearly unsustainable state of affairs. Despite many earlier attempts at reform endemic problems remained. George Soros described the company as "a black hole in the budget and a major source of corruption".[80]

High stakes were involved in any reform plan. The new government nonetheless had little choice but to press ahead.

With the help of the EBRD and other international organisations that had been involved in policy dialogue with the Ukrainian authorities, a plan soon emerged to reform the gas sector and modernise its infrastructure. In the short-term, help could be provided by rehabilitating the transmission network and improving energy security through gas purchase financing support.

By December, a first EBRD loan was agreed with the Ukrainian government to repair and upgrade the gas transmission system. At the same Board

---

79 This section draws on an interview with Gian Piero Cigna in 2021 and an article, G. P. Cigna and S. Sheremeta, 'Lessons from Naftogaz', *Ethical boardroom,* 18 June 2019 https://ethicalboardroom.com/lessons-from-naftogaz/.

80 George Soros, 'Wake up, Europe', *The New York Review,* 20 November 2014, https://www.nybooks.com/articles/2014/11/20/wake-up-europe/.

meeting where the loan was approved, a paper called 'Ukraine: Reform Anchoring and Crisis Response Package' was also discussed. It looked forward to developing "a financing structure to facilitate imports of gas from the Western [EU] route important to the diversification of Ukrainian [sources of gas] supply". This became a larger financing for gas purchases the following year.

The loans first involved the transmission operator, Ukrtransgaz (UTG), a subsidiary of Naftogaz, and then Naftogaz itself (as described in Chapter 5). However, the key condition of the UTG loan, reinforced in the loan to Naftogaz that followed, was the implementation of a comprehensive reform of their corporate practices under EBRD guidance.

The process began in early 2015 with the EBRD leading a review of Naftogaz's corporate governance which was completed in June. Problems were legion. According to Cigna, who led the work:

> On paper the company was generally aligned with legislative requirements, but the practice was well behind. We ran two parallel reviews: one on the company's practices and one on the legislation governing these practices.
>
> What we discovered was astonishing. The board was there, but had never met in the last 24 months. There was a lack of clarity on who owned and who decided what. The governing framework was extremely complex with a myriad of norms often conflicting with each other. There was political interference at all levels, no risk management or other internal controls like internal audit and compliance functions, and if the company wanted to buy some paper four or five signatures were needed, yet some substantial operations were conducted with no process at all!

The comprehensive review showed not only a long list of practices within the two companies that needed to be addressed, but also several changes to legislation that impinged on the companies that would allow the proposed reforms to be effective.

Among the priorities identified were the need to reduce state interference with the company's management, clarify the group's ownership structure, provide commercial autonomy through separating ownership, regulatory and policy-making functions (which would also reduce conflicts of interest), establish an independent and qualified supervisory board, strengthen internal controls and develop a group strategy. There was a need

too at ministerial level to introduce a 'state ownership policy' which could define the rationale behind state ownership.

The scale of the task was huge—necessitating amendments potentially to more than 80 laws, decrees, orders and instructions.[81] It took three months of negotiations before the Cabinet of Ministers approved the Naftogaz Corporate Governance Action Plan on 21 October 2015.

The first stage of the plan, allowing Naftogaz to operate as a commercial company free from political interference, was implemented quickly. The company's shares were transferred to the Ministry of Economy, clarifying ownership, but without taking on responsibility for operational policy or management which remained with the company. A revised company charter, with terms of reference for the supervisory and management boards, was also approved in December that year.

The changes paved the way for the release of finance from the second EBRD loan and, as agreed under the terms of the loan, purchase by tender in line with best European practices of more than 1 billion cubic metres of gas during the non-heating season for storage in time for the following winter.

Naftogaz's supervisory board was appointed in April 2016, the first board of a Ukrainian state-owned enterprise to be made up of well-qualified and independent directors.

The road ahead was a rocky one nevertheless.

Naftogaz had yet to fully meet the OECD Principles and Guidelines for Corporate Governance of State-Owned Enterprises, the ultimate goals of the EBRD-inspired action plan. Changes of ministers and a new government in April 2016 interrupted the reform process and a series of departures culminating in the dramatic resignation of the whole of Naftogaz's supervisory board in September 2017 made it clear that reform remained a complicated process. The outgoing chair of the board laid the blame with politicians in a statement: "Despite assurances from senior politicians, deadlines have passed and commitments have not been delivered, with an environment of government control not envisaged in the corporate governance action plan."

---

81 Key changes made with the EBRD's help were amendment to the law on joint stock companies to introduce the concept of independent directors in 2015, a law requiring supervisory boards to have at least a majority of independent directors in 2016 and a new law in 2018 which included a provision to prevent a general shareholder meeting from deciding matters reserved for the supervisory board (removing a historic problem seen in Ukraine of bypassing the board).

By November, however, following efforts by the international institutions including the EBRD, and by the Government, a new well-qualified supervisory board was approved by the Cabinet of Ministers. Gradually, further corporate governance improvements were made. Notably, the Government approved the ownership policy of Naftogaz—one of the key documents under the OECD Guidelines—and a new company charter more in line with the Guidelines was introduced in October 2020.

Naftogaz itself acknowledges the CGAP has yet to be fulfilled and that more corporate governance reforms are needed, including to state-owned enterprises more widely. More improvements are being planned.[82]

Some reflections on corporate governance

For Cigna, looking back in 2021, there were lessons from the Naftogaz experience:

> Naftogaz was a page-turner. From this, and 17 years of work on legal reforms and corporate governance, I believe three essential elements are needed for effective reform: pressure, reward and the right culture.
>
> Clients need to feel pressure from covenants, domestic policy discussions and the voice of IFIs, otherwise the risk is that they do nothing.
>
> Reward—in the form of "name and shine"—brings a demonstration effect and encourages wider reform.
>
> Changing the culture is the most challenging of the three. It needs support from the top—from policymakers to company boards and management—and it takes a long time to get there. But all three need to be there for success.
>
> And maybe I can add another element that's needed: perseverance!

Conclusion

The private sector nature of the EBRD, and its focus on operations, encouraged an effort to improve governance at the corporate level where it was sorely needed.

82 For details, see the Naftogaz company website, https://www.naftogaz.com/www/3/nakweben.nsf/0/9D3499C093EF79EBC2257F38004FA269?OpenDocument&Expand=1&.

In parallel, in its engagement with the authorities of its countries of operations, including in exercising its political mandate, the Bank's interventions were focused on assessments and policy dialogue.

It was the deeper understanding of the importance of high-quality institutions, and the role they played in making markets work well, that drove the effort by the Bank to tackle governance at a higher level and seek a more business-friendly investment climate.

The EBRD succeeded as a trusted partner and brought public and private players together to engage on market and business issues more effectively. This led to many changes with practical benefits. Pressure from the Bank to introduce independent arbiters—ombudsmen and regulatory bodies—to help tackle market inequities and state-led interference was similarly beneficial.

Behind these changes frequently lay the work of specialist lawyers who helped to introduce and amend laws which raised standards and reduced investor nervousness. Markets cannot work in a vacuum but depend on clear rules, well applied. Their legal underpinnings were well-served in many countries of operations through the dedicated work of the EBRD's lawyers, both in the legal transition team but also on the operations side as companies in the EBRD regions learned to appreciate the value of legal protections offered by sound processes.

On the financial markets side too, the Bank's legal teams played an important role in improving the regulatory landscape. But it was the pooling of expertise from across the Bank to promote the use of local currency and to strengthen money and capital markets that galvanised changes here.

Many novel instruments—from various types of bonds to new interest rate benchmarks—were introduced, alongside specialist advice on financial market structures and regulations. Because the EBRD took risk on its books and made investments as well as giving advice—"putting its money where its mouth was"—it had a market credibility that was unmatched by others in its regions.

The goal of improving countries of operations' financial infrastructure and range of financing options was to enable them to achieve a greater resilience to unexpected shocks. On the governance side too, the aim of a better investment climate and clearer responsibilities and accountabilities for market institutions was designed to raise economic performance.

The extent of success in these endeavours is not easy to pin down. Improving resilience and governance is a massive task and there is clearly more to

do. Steering through the current Covid-19 crisis, and recovery from it, will be a stern test. The issue of climate change, discussed in the next chapter, is perhaps an even bigger one. But only resilient and well-governed market economies have the best chances of coping with the challenges.

Chapter 9

A Better Climate

Introduction

From its earliest days, the Bank paid close attention to its environmental mandate.[1] Much of the initial effort was devoted to the formulation of policies to ensure there were no adverse environmental impacts from its projects, a "do no harm" approach. Management was also concerned with mitigating the risks surrounding nuclear power and waste.[2]

The grim environmental legacy of the Soviet period and the nature of the EBRD's investments in industry, transport and power meant a focus on energy efficiency improvements was an obvious route for the Bank to take as it developed its business activities.

Tackling energy efficiency fitted well with improving the performance of enterprises. It was also relevant to the growing interest in the issue of global warming. However, the international debate on climate issues was still in its infancy in the early 1990s.

The first Intergovernmental Panel on Climate Change (IPCC) in 1990, ahead of the Rio Earth Summit in 1992 which the EBRD President attended,[3] introduced the UN Framework Convention on Climate Change (UNFCCC). Yet it was only after the first Conference of the Parties (COP) in Berlin in 1996, and the publication of the second IPCC report, that the climate scientists formally declared for the first time that global warming

---

1 As expressly provided in Article 2.1(vii) of the Agreement Establishing the Bank.

2 See Kilpatrick, *After the Berlin Wall,* Chapter 9, 'Nuclear Safety'.

3 See Kilpatrick, *After the Berlin Wall,* Chapter 8, 'Environment Matters', p. 223.

was probably caused by humanity. Despite the verdict of over 2,000 experts,[4] this conclusion remained a subject of considerable controversy.

The Bank's approach in those days, while consistent with mitigating climate change, was rather more oriented towards dealing with the region's legacy of high energy intensity and environmental risks than designed to pursue wider climate goals. It was after the G8 Gleneagles Summit in 2005 that the Bank's emphasis shifted towards climate change in a focused and strategic manner.

A series of initiatives beginning in 2006 led the Bank to conduct a wide range of climate change related projects and to build climate mitigation and adaptation activities into its private sector-oriented business model. In parallel, its policy work and increasing presence on the global stage raised its profile as a leading exponent of climate action.

By 2019, three decades after the idea of the EBRD was born, green finance reached 46 per cent of total Bank investment, close to €5 billion, with a target set the following year of becoming a majority green Bank by 2025.

From its founding President, Jacques Attali, to Odile Renaud-Basso, the latest to hold the position, EBRD Presidents have committed to strengthening the Bank's environmental goals. As a result, the EBRD today stands at the forefront of global efforts to develop a low carbon transition through its work in its countries of operations and its private sector focus.

1. Early Efforts to Improve Energy Efficiency

The inefficient use of energy and neglect of environmental impacts across the EBRD region was a substantial legacy of the communist era. According to a 1995 Energy Operations Policy[5] paper, most countries used between three and five times more energy per unit of value added than western industrial countries. Even the best performer, Hungary, used about twice as much energy per unit of GDP as Germany while in the case of Azerbaijan the multiple was a factor of ten.

Unfavourable climatic conditions in many countries of course did not help—though should have been a spur for greater efforts towards

4 IPCC Second Assessment, 1996, p. viii.
5 'Energy Operations Policy', 13 March 1995.

efficiency—but the concentration on heavy industry (another Soviet legacy) and use of inefficient and outdated technologies were the main culprits. These weaknesses were made worse by exceptionally low energy prices—on average across the region, energy prices were estimated to be around one-quarter of the average of western industrial countries—and the prevalence of subsidies and social welfare norms that had built up during the communist era. On top of this, the central planning system had distorted incentives and failed to provide a business environment conducive to investment in modern or alternative technologies.

The immediate problem in the years following the collapse of the Soviet Union was to find ways of keeping economies functioning in the face of unprecedented change. From an energy perspective this meant reducing disruptions and stemming network losses. Assistance was also needed to commercialise power and heating suppliers, improve bill collection, reduce arrears and integrate energy systems and markets.

An energy efficiency team

During the 1990s, growing interactions with public enterprises, municipalities and utilities, which were major energy consumers, soon led to the realisation that the Bank could do more to address the demand side of energy use, where Bank financing could also facilitate greater efficiency. A gap existed in the market that was beginning to be filled by foreign investors—and several bankers believed the EBRD could facilitate and accelerate this process.

With the strong support of President de Larosière, a small independent team was set up around the middle of the decade within the Energy Group to pursue energy efficiency banking projects more directly and build up the Bank's capacity in this area.

The Bank's private sector mandate, in the face of the dominance of public sector enterprises, meant innovative approaches were needed. The team focused first on developing relationships with energy service companies (ESCOs), and then on municipal district heating systems.

Energy service companies and district heating

As with other sectors during this period, the EBRD was well placed to support western investors interested in expanding into new markets in central

and eastern Europe. Among them was Honeywell, a multinational US company selling energy control systems and services for buildings and industrial production processes (including utilities). The company, like some of its competitors at the time,[6] was keen to develop an integrated energy service business through energy performance contracting (EPC) and saw the EBRD region as one of its strategic targets.

In each EPC, the sponsor guarantees that the resultant energy and operational savings will cover the project costs. The novelty of this arrangement in the new region appealed to investors who envisaged central European countries moving towards this western business model and it fitted neatly with the EBRD's transition objectives.

The EBRD's energy efficiency bankers teamed up with Honeywell (and others in similar projects) under a multi-project facility for public and private sector entities in the region. This seemed a useful way of delivering energy efficiency savings in a situation where clients were unable to raise debt themselves but where the value of the energy savings paid for the costs of the ESCOs' investment and rewarded them financially. It also allowed the EBRD to tap into a higher number of small investments in the sector than it would have been able to manage on its own and had the potential to promote private sector development through a demonstration effect of successful ESCOs.

Towards the end of the decade, the energy efficiency team turned its attention towards municipal district heating systems and energy savings in the public sector. District heating provided a large share of the heating supply market in many EBRD countries and was ripe for energy improvements. There was a widespread need to modernise the typically inefficient, coal-fired plants involved which were highly polluting and emitted significant amounts of greenhouse gases (GHGs), and to upgrade boilers and other infrastructure.

In a typical case, a sponsor would bid in a municipal tender to operate a district heating plant and then improve it and the network on a turnkey basis, imposing tight controls over costs and collection procedures.

The resulting efficiency improvements—losses could often be reduced by a factor of three or four in the case of boilers, and much more in relation

6 Dalkia, part of the French-owned Vivendi group, was one such company with which the EBRD did similar business; Landis and Stefa (previously Landis and Gyr), part of Siemens, was another.

to transport—were designed to be sufficient to repay the investment and financing costs without tariff increases.

In the wider context, efforts made by the Bank helped to bring municipal district heating systems closer towards commercial viability. This required that tariffs reflected full cost recovery with charges based on usage and affordability. It meant the Bank was able to ensure energy use was more efficiently managed on both demand and supply sides.

The energy efficiency team also started to support energy audits in private companies. These audits identified opportunities for energy efficiency gains and analysed their financial returns as a basis for defining potential energy efficiency components.

Despite the clear transition and economic logic of these approaches, the energy efficiency team's business was slow to take off and its growth did not compare well with the efforts of the wider infrastructure group which concentrated on large-scale power projects. The difficulties for the team were mounting.

In the case of ESCOs, where the Bank held equity, the procedures were complicated and involved a lot of senior management time checking the procedures and business plans of small and transient project companies. By 2001, 12 ESCO projects had been signed but were underperforming with weak profitability.

Growth of the team's business volume, a key measure of success within Banking, was being squeezed by the early 2000s. Some new thinking on how to deploy the skills of the energy efficiency team was needed.

Energy efficiency in industry and infrastructure sectors

The replacement of obsolete equipment reduced energy costs and improved the competitiveness of local industries directly. It also positioned them for the future as energy prices rose towards international levels. Whether through investments in the operational restructuring of industrial enterprises or in projects to rehabilitate and modernise power plants, oil and gas equipment or railway rolling stock, the Bank developed an approach to improve energy efficiency. But it was often difficult to integrate in projects as it added complexity to project preparation and required additional time from staff focused on getting projects signed.

On the supply-side, activities involved rehabilitation and modernisation of power plants and advice on market reforms, particularly on energy tariff

setting and how to apply economic criteria. Energy efficiency improved with the introduction of new turbines and other modern equipment and with improvements in the functioning of power systems and their markets. But it was slow going. Finance was lacking, understanding was poor, interests were not always aligned and a shortage of qualified engineers and accountants created bottlenecks.

Improvements in energy production and the replacement of old plant and equipment in industrial enterprises were often achieved with advanced imported technology which was far more energy efficient. Safety was improved through advice and the use of suitably qualified engineers. Years of underinvestment and a financial system that was incapable of providing long-term finance allowed the EBRD to make a significant contribution. In doing so it raised energy efficiency and improved safety.

The emergence of Sustainable Energy Financing Facilities (SEFFs)

A leading banker in the energy efficiency team, Terry McCallion, growing impatient at the slow progress decided to branch out and join the Financial Institutions team. He was aware how business there had recently taken off to reach a wide range of companies through the provision of credit lines to partner banks for on-lending to small businesses. He began exploring the possibility of replicating the SME lending model in some way for energy efficiency investments.[7]

Shortly afterwards, a new country strategy was due for Bulgaria and this provided an opportunity to explore his idea in a country context. It was a good choice since the EBRD had established strong relationships with local banks and Bulgaria was one of the most energy intensive countries in the Bank's portfolio with an energy intensity about twice that of Poland and Romania (themselves well above the EU average).

Bulgaria was also looking to improve its energy performance as part of the EU accession process (negotiations began in March 2000). Improving energy

7 Early precursors to the approach were two projects in 1996. One was with state-owned Romanian Commercial Bank, which involved a small credit line for on-lending to SMEs and for energy conservation projects. The line was supported by EU PHARE investment grants. The other was a small loan to Priemyselná Banka A.s. Košice (PBK) in Slovakia, part of which was to support energy efficiency improvements. Another early project was with Hungary Budapest Bank, which involved an EBRD-PHARE Environment and Energy Efficiency Co-Funding Scheme.

efficiency was a strategic priority for EU entry and EU compatible standards and legislation were being introduced for industry energy consumption, combustion processes, building standards and household appliances.

Some other factors weighed in favour of Bulgaria as a good first target. In 2003, the State Energy Regulatory Commission increased energy prices by 15 per cent and a new Energy Act was passed in November. Designed to comply with the EU Energy Chapter, feed-in tariffs were set to encourage the development of renewable energy with the aim of an 8 to 10 per cent share of energy production by 2020. An Energy Efficiency Act obliging high energy users to conduct energy audits and energy saving programmes followed.

Furthermore, the commitment as a condition of EU entry to decommission units 1-4 of the Kozloduy nuclear power plant by 2006—which contributed approximately 12 per cent of Bulgaria's energy output—had given rise to an international decommissioning fund[8] to help mitigate the consequences, which included a window to support energy efficiency and renewable energy.

This component of the support fund proved to be an important factor in overcoming barriers to energy conservation and to enable a first EBRD financing facility, the Bulgarian Energy Efficiency and Renewable Energy Credit Line Framework (BEERECL), to be prepared with partner banks to deliver energy improvements.

A grant of €10 million under this window was agreed in December 2003 by the Kozloduy International Decommissioning Support Fund (KIDSF) assembly of donors. This was used in the facility to incentivise banks and sub-borrowers to consider energy efficient solutions. Banks had no technical expertise for investment appraisal and risk assessment in this field, lacked information and misperceived the risks of energy conservation. Nor did they possess relevant marketing capabilities and faced additional costs from appraisal and monitoring. To compensate for the costs and risks involved they were offered a one per cent annual administration fee on disbursement amounts.

Sub-borrowers likewise had a poor understanding of the potential benefits, including from likely future energy tariff increases, and lacked dedicated in-house energy management expertise. Businesses typically focused on core short-term objectives and managers preferred expansion investments over those that saved costs. They were offered generous rebates on

8 The Kozloduy International Decommissioning Support Fund (KIDSF).

expenditures for energy efficiency and renewables' projects. Consultants, paid for from the grant funds, assisted with project and loan preparation and gave advice on matters like the cost-effectiveness of different measures and appropriate energy management strategies.

The first BEERECL framework was agreed in January 2004 and involved two partner banks, United Bulgarian Bank and Bulgarian Post Bank, with €50 million made available for on-lending to the private sector for energy efficiency and small renewable projects. It covered a wide range of projects from the introduction of heat recovery systems and automation to run-of-the-river, biomass, geothermal and other renewables investments.

The pilot framework's success persuaded several other banks to join the facility and it was extended over the years, with later versions reducing the scale of the incentives and aligning them more closely with energy savings, a major target of the facility. A version of the framework which focused on residential energy use followed soon afterwards.

Before long, similar facilities, which were called Sustainable Energy Finance Facilities (SEFFs),[9] were deployed in many countries across the region, from Ukraine and Moldova to the Western Balkans and to the Caucasus and Central Asia. The approach was successful in scaling up EBRD activities and improved energy utilisation among a large number of small businesses and industrial companies; and helped to reduce market barriers holding back the energy conservation market.

The main purpose was to create markets for energy efficiency and renewable energy financing rather than directly reduce energy intensity—individual sub-projects prevented worthwhile but generally limited amounts of carbon emissions. The hope was that larger-scale energy savings would occur by virtue of demonstration of profitable opportunities derived from reduced energy use, and that raising awareness and skills in banks would lead to their own lending capacity for similar projects.

The approach succeeded in extending energy efficiency activity, especially to SMEs and some households, but was not enough at that stage to answer the question posed by the G8 to MDBs in 2005 soon after the initiative started.

---

9 The first SEFF was deployed in Slovakia in October 2007. Known by its acronym of SLOVSEFF, it was a €60 million credit line to four Slovakian partner banks (VUB, Slovenska Sporitelna, Dexia Banka and Tatra Banka) for on-lending for private sector industrial energy efficiency and renewable energy projects and for residential energy efficiency projects.

2. The Gleneagles Summit

The Kyoto Protocol agreed in 1997 committed industrial countries to reduce greenhouse gas emissions. However, ratification took place only slowly, or not at all in the case of the USA. It signed the Protocol in 1998, did not ratify it and dropped out of the process in 2001. The Protocol came into effect early in 2005 but the absence of commitments by the USA and China—the biggest emitters—reduced the potency and effectiveness of the original agreement. Global emissions continued to accelerate following Kyoto.

Ahead of the 2005 G8 Summit, a great deal of attention was being paid to providing debt relief for the poorest African countries. Large (and sometimes violent) demonstrations by people committed to putting the spotlight on poverty were taking place. As the G8 leaders' meeting approached, the campaign 'Make Poverty History' was increasingly vocal.

It was the UK government's turn to host the annual G8 event. It was to be chaired by recently re-elected Prime Minister Tony Blair and to take place in July at Gleneagles, a golf resort near the Scottish Highlands.

Blair was facing a difficult moment. Prospects for a deal on Africa were in the balance. With the world's attention galvanised by Bono and Bob Geldof's presence in the 'Make Poverty History' campaign, failure would have been particularly humiliating. Blair's other main hope for the agenda—progress on climate change—was also looking over-optimistic, despite his good relationship with the US President, George W. Bush.

Early on the first morning of the Summit, as Blair and Bush held a bilateral discussion over breakfast, news came in of a terrorist bombing in London. The seriousness of the incident, in which 54 people lost their lives, might have wrecked the whole event. However, the G8 leaders, seeing the need to stand together in the face of terrorist attacks, made efforts to find compromises to allow the Summit to reach positive conclusions, including on climate change.

The Summit's conclusion on climate change was notable for bringing the USA a little closer to the mainstream view that human activities were a major cause of climate change. It helped to reinforce the conclusion that actions to slow the progress of global warming were needed even more urgently than foreseen a decade or so earlier.

At a press conference at the end of the Summit, Blair put his perspective on the result:

> What it is however is a firm consensus that this problem needs to be tackled, has to be tackled now, ... with ...a plan of action that brings ...the major wealthy economies, including America, and ... the emerging economies of China, and India ... together. That I think is something to be proud of.

The final G8 Summit statement emphasised the need for action:

> We face serious and linked challenges in tackling climate change... [and] we will act with resolve and urgency now to meet our shared and multiple objectives of reducing greenhouse gas emissions...[10]

The G8 also saw a major role for MDBs in helping borrowing countries respond to the challenge of climate change. The G8 Gleneagles Plan of Action on Climate Change, Clean Energy and Sustainable Development invited the World Bank and other MDBs to put forward specific proposals on the topic. They should "make best of use of existing resources" to accelerate clean energy-technology adoption, increase investments in the sector, identify "less greenhouse gas intensive growth options and ensure that such options are integrated into Country Assistance Strategies" and "develop local commercial capacity".[11]

It was a comprehensive appeal to the MDBs to get engaged in climate action.

3. Towards a Sustainable Energy Business Model

When EBRD President Jean Lemierre returned after the summer break in September, he turned his attention to the upcoming Capital Resources Review (CRR3) which covered the period 2006-2010 and was due for approval at the next Annual Meeting in May 2006.

The Bank had been performing well, and once the timing of EU countries' graduation had been agreed, its focus for the period would be on efforts to move 'south and east' after launching an initiative in 2004 aimed

10 UK Government press release, London, July 2005. G8 Statement on 'Climate Change, Clean Energy and Sustainable Development'.

11 UK Government press release, London, July 2005. 'Gleneagles Plan of Action on Climate Change, Clean Energy and Sustainable Development'.

at Early Transition Countries.[12] That was a transition direction of note but a more dramatic or optimistic forward-looking centrepiece was lacking for the Annual Meeting.

Josué Tanaka, a senior banking director, was in charge of corporate strategy and had been pulling together the different strands of work for CRR3. The exercise examined in exhaustive detail the Bank's performance, prospects and future requirements. Nonetheless, the need for a positive focal point to the meeting was also on his mind.

At a senior management meeting to discuss preparations for CRR3, the President asked in passing how the EBRD could respond to the Gleneagles' Action Plan. The G8 statement had asked explicitly for specific proposals to be put to MDB annual meetings, but few around the table had yet factored this prominently into their thinking.

Tanaka, a Princeton graduate and MIT[13] PhD with a penchant for jazz drumming that matched his energy level, was well-suited to come up with a response. He had been at the Bank since its earliest days and understood how the EBRD had many times before successfully, and quickly, met G7/8 requests.

Later that month he realised all of a sudden that he had an answer to the G8's call which presented a great opportunity to place the EBRD at the forefront of climate action, as well as offering a solution to the Annual Meeting dilemma. The Bank had many elements which could be combined to develop and implement an ambitious and practical approach, he reasoned. It had the ability to work with both the private and public sectors, it could combine energy conservation and clean energy investments with technical assistance and policy dialogue and was able to design systems that could improve markets, raise incentives, strengthen regulations and cut greenhouse gas emissions. The experience of the energy efficiency team combined with the sectoral and country expertise developed by the Bank in its first 15 years provided a strong base to define a bold initiative for the next strategic period.

In those days, Lemierre had an open door for staff keen enough to come by at 7.30 in the morning. On the last day of September, after a sleepless night drafting a note on how the Bank could respond to the G8 call, Tanaka

12 The Early Transition Countries Initiative (ETCI), see Kilpatrick, *After the Berlin Wall*, Chapter 12, pp. 329–332.

13 Massachusetts Institute of Technology (MIT).

decided to present his idea to develop a Climate Change and Energy Efficiency Initiative, as part of CRR3, to the President.

Six months was a short time to develop a coherent climate initiative for the Annual Meeting, potentially involving large parts of the organisation. Nonetheless, the skills and instruments to deliver results were there and Tanaka was betting on the EBRD's agility and its staff's commitment and drive to succeed. Lemierre understood and agreed that he should press ahead.

There were, as Tanaka saw it, two requirements for success. First, there would need to be full buy-in to the idea by the Bank's top management since the initiative was likely to touch every department in one way or another. And second, to deliver credible action at scale on climate change, the initiative would need to be mainstreamed across the Bank, so that every banking team would have good reasons to step up its activity on energy efficiency, renewables and other climate-related investments and be ready to conduct policy discussions with authorities. With the EBRD's help the private sector would be able to deliver climate-friendly results.

Mainstreaming

A first action Tanaka reasoned, to the puzzlement of those hearing rumours of a new initiative on climate change, was to cease the direct finance activity of the energy efficiency team and redeploy several of its staff to other sector teams. This allowed a newly-formed Energy Efficiency and Climate Change (E2C2) team to focus on technical and policy innovation, while having sector teams take on the processing of financial transactions.

The new E2C2 team developed a range of programmes supporting energy efficiency projects in large energy-intensive industries, in SMEs, in the power and transport sector, and in urban infrastructure. Team experts in this central unit reporting to the First Vice President supported colleagues across sectors and countries to develop a pipeline of projects within each of these programmes.

With the scope for engagement now improved, new business lines were found as energy efficiency experts identified opportunities within each sector and introduced innovative business products combining technical advice and finance. As the mainstreaming of energy efficiency work expanded, demand for advice grew quickly and with it the team of E2C2 experts.

The second step was to reinforce this activity by encouraging all bankers to consider optimisation of the use of energy as a real, and for many, a new business opportunity—whether to enhance profitability, introduce and improve products, raise competitiveness or all three—rather than treat it as an environmental activity unrelated to the core business of the Bank.

Bankers soon realised they could enhance their relationships with business clients by using the energy efficiency experts who were able to offer their businesses energy audits and ideas for operational improvements and reduced costs. The very poor use of energy in the EBRD region meant there were many opportunities.

The creation of a central expert resource to be used in a cross-cutting way and mainstreaming the initiative across the Bank with strong high-level management support gave impetus to the initiative from the word go.

Above all, it would establish climate change activities as a core business for the Bank.

4. The Sustainable Energy Initiative (SEI)

The need for deeper action

Three separate challenges needed to be addressed which provided strong reasons for intensified action: improvements to competitiveness, the need for energy security and the role of the transition countries in helping to meet Kyoto targets as Annex 1 countries.[14]

Many enterprises in manufacturing and other industrial sectors in the region had positioned themselves as low-cost producers when the transition began. They were facing increasing competition from East Asia, where labour costs were even lower, but also cost pressures from rising energy prices. Low energy costs had more than offset the inefficient use of energy, but as energy prices climbed towards international market levels—where oil prices had tripled between the end of 2001 and early 2006—this benefit was being eroded. Pressures on energy-intensive producers were growing rapidly. An increased effort to cut energy waste could help maintain

14 Annex 1 countries were industrialised countries committed to reducing emissions under the Kyoto Protocol.

competitiveness and improvements in productivity went hand-in-hand with the Bank's agenda for reform, including the goal of liberalising the energy sector.

Most countries of operations depended on oil and gas imports, with inefficient use unnecessarily absorbing (often precious) foreign exchange. Energy security could be improved by reducing energy waste, changing the fuel mix, diversifying sources and increasing cross-border cooperation (a frequent source of tension). This was less true though of energy-rich countries, such as Azerbaijan or Russia, which benefitted from higher oil and gas prices.

The waste of energy in the EBRD region made it one of the most attractive areas in the world to target from a greenhouse gas perspective. The transition economies, after the USA and China, were among the highest greenhouse gas emitters with total emissions amounting to 13 per cent of the global total. Russia, Ukraine and Poland featured in the top 25 global emitting countries at this time, while Ukraine and Uzbekistan showed the highest carbon intensity.

Russia's energy intensity was also high and about twice that of the USA and China (and three times that of Germany, Japan and India). As the largest economy in the EBRD region, Russia was an important target for improvements in its use of energy. One of the areas in which the EBRD was making significant investments was Russia's power sector. This was the largest in Europe and had very poor average thermal efficiency.

Although GHG emissions in the region dropped with the sharp decline in economic growth in the early years of transition, they had risen strongly in the 2000s and the International Energy Agency (IEA) predicted a large increase ahead. With the majority of the region's emissions coming from Annex 1 countries, there was every reason to curb the region's high energy and carbon intensities, support a lower carbon path and contribute to the global task.

The launch of the SEI

The Sustainable Energy Initiative (SEI)—what Tanaka had originally pitched as the Climate Change and Energy Efficiency Initiative—was presented that May to the Board of Governors as the EBRD response to the G8 call. While in other regions climate action would focus on tropical forests' protection or on finding lower carbon solutions to respond to sharp rises in

energy demand, energy efficiency was the main contribution which the original EBRD region of operations could make to climate action. Accordingly, the focus was mainly on mitigation. The SEI provided a framework covering a range of sectors and financing instruments to accelerate the adoption of new, cleaner technologies.

The EBRD's pursuit of market discipline, and its actions to address supply and demand-side inefficiencies, was central to its approach and persuasive arguments for Governors. Its regional knowledge, capacity to work with the private sector and proven set of operational products helped with planning the initiative quickly.

Management pointed to the fact that the Bank had already invested around €1 billion in the previous four years in projects directly reducing carbon emissions and in power projects with climate change benefits.[15] There had been many beneficiaries. Among them were industrial projects targeting improved energy efficiency in energy-intensive sectors such as steel, aluminium, chemicals, pulp and paper and cement; renewable energy investments; credit lines to banks for energy efficiency on-lending; municipal district heating projects, including their commercialisation and improved tariffs; and public transport investments in new trams and buses, light rail systems and traffic management and control systems.

The SEI would build on the EBRD's abilities to deliver climate-friendly solutions and advice. In particular, the volume of investment in energy efficiency and renewables was expected to increase and it aimed to build local commercial capacity to promote sustainable energy objectives. There were opportunities too to explore the new area of carbon trading as a market-based instrument for environmental action. The initiative lined up well with the plans for 2006-2010 under CRR3, also discussed at the Governors' meeting.

The reaction of the Governors when the initiative was presented to them on 22 May 2006 was positive. Hilary Benn, the UK Minister for International Development, said he appreciated "the EBRD's work ... to take forward the G8 commitments made at Gleneagles last July. We very strongly support the ... Initiative" while European Commissioner for Economic and Financial Affairs, Joaquín Almunia, commented:

---

15 GHG reduction was estimated at 2.7 million tonnes of CO_2 equivalent a year, and around one-third of a billion tonnes of oil equivalent. 'Climate Change and Energy Efficiency Initiative', p.5, 5 May 2006.

> We believe this to be a very promising contribution to the IFIs' global endeavours undertaken in response to the G8 call at Gleneagles, making good use of the Bank's acknowledged expertise in the environmental field and its extensive operational experience in the region. We very much welcome this wide-ranging Initiative …"[16]

Lemierre at his press conference after the meeting acknowledged the "very strong support" and in particular from countries of operations: "They all mentioned that it is crucial for them."[17]

The SEI would prove to be a stepping stone for the future direction of the EBRD.

Delivering the SEI

A goal of doubling the pace of energy efficiency and climate change activity was set, targeting investments of up to €1.5 billion over the following three years (2006 to 2008) for an estimated total project investment value of €5 billion.

As the largest single international investor in the private sector of many countries of operations, the EBRD initiative was expected to mobilise significant private sector financing for industrial investments and public-private partnerships for infrastructure projects. Donor funds were needed for technical assistance on energy audits, feasibility studies, training and advice on regulatory frameworks and for incentives, and to limit the effects on poorer households from commercially-based energy tariffs.

The Bank's track record of mobilising and managing donor funds and programmes on energy efficiency—of which the EU was by far the largest contributor but with significant amounts also provided by Japan, the Netherlands and Switzerland—had already yielded a high investment leverage ratio of donor funds and provided a valuable basis on which to scale up this funding.

The Bank was able to deploy a wide range of financing instruments, and its co-financing capacity, to reach its investment target. This included both private and sovereign loans but also sub-sovereign lending, which was especially important in tackling energy and resource efficiency problems at the

---

16 Governors' speeches at the 2006 Annual Meeting.

17 Press conference, 22 May 2006.

local level. The Bank's ability to provide equity directly or through equity funds was also valuable though was not used very frequently. It became more relevant later with the rise in renewables activity, particularly in projects involving wind and solar power.

Not long after the SEI got underway a landmark report on climate change was published on 30 October 2006. Its principal author, former EBRD Chief Economist Nick Stern, had joined Chancellor of the Exchequer Gordon Brown's Treasury after returning to the UK from his position as Chief Economist at the World Bank. Following the Gleneagles Summit, Brown had asked him to review the economics of climate change.[18]

The Stern Review, which became hugely influential in subsequent debates, concluded that dramatic and immediate action was needed to stave off a sharp rise in average world temperatures which would otherwise cause serious global economic harm and social disruption.

The ensuing spotlight on climate concerns boosted the role of the SEI and fitted neatly with the EBRD's claim to be among the first international institutions to tackle the climate change issue in a holistic and systemic way.

The SEI was indeed a success. In terms of the first objective—a doubling of the pace of investment in sustainable energy projects—the total amount the EBRD invested between 2006 and 2008, €2.7 billion, greatly exceeded the €1.5 billion target. It involved 166 projects for a total project value of €14 billion, also well above target.

The more direct involvement of banking teams across sectors and countries in SEI projects and products, supported by expert advice from E2C2, worked well. Donor partnerships also provided substantial sums towards technical assistance and grant co-financing. Projects were implemented in 24 countries, the majority of them early or intermediate transition countries, with the largest concentration of projects in Bulgaria, Georgia, Russia and Ukraine. Nine sectors were covered, with municipal and environmental infrastructure the largest by number at around 28 per cent of the total, followed by lending to local banks (19 per cent) and power and energy and the agribusiness sector with about 15 per cent each. The biggest investments by value were in power and energy (43 per cent) followed by general industry (17 per cent).

---

18 'The Economics of Climate Change: The Stern Review', 30 October 2006. Stern had previously acted as Director for Policy and Research for the Commission for Africa, organised by the UK Government as part of its preparations for the 2005 G8 Summit.

Energy savings were not specifically targeted at this stage, but an Evaluation Department estimate[19] showed that the greatest contributions came from power and natural resource projects. The pattern in terms of GHG emission reduction was similar, except here general industry provided as much to the overall reduction as natural resource projects with each making about half of the contribution from power and energy operations.

A Special Study by the Evaluation Department in 2010 declared the SEI "successful" since it made a "real and positive contribution to transition impact and … sustainable development" and it commended the banking and E2C2 teams for their "innovative and proactive approach" in implementing its objectives. The report noted that transaction responsibility remained with the respective banking teams, with E2C2 providing technical support in defining and driving the development of SEI activity in each sector. As such, it was "market-based" and an "important lesson" (which the Evaluation Department supported) was that SEI activities were "perceived as business opportunities rather than promoted … on a compliance perspective."[20]

This was an important conclusion and validated the approach Tanaka had initiated.

5. SEI Phase 2

Encouraged by the success of SEI in the first three years, Tanaka, working with new First Vice President Varel Freeman, began to prepare a second phase before the SEI came to an end in 2008 to run from 2009 to 2011 and aimed to present this to Governors at the 2009 Annual Meeting. The financial crisis, which started in late 2008 could have thrown the effort into disarray, but the initiative was now embedded in the Bank's overall approach—SEI business volume had reached almost 20 per cent of the Bank's total.

In some respects, the economic shock helped the Bank to redouble its efforts in tackling climate change. Not only did countries of operations need financial support in the aftermath of the crisis but its impact was severe, for example, on the nascent carbon trading market with this promising route

19 'Special Study on the Sustainable Energy Initiative Phase I Strategic Review', Table 7, p. 13 and Table 10, p. 16, EBRD Evaluation Department, October 2010.

20 'Special Study on the Sustainable Energy Initiative Phase I Strategic Review', p. 1.

forward now limited. Energy efficiency measures became an even clearer viable short to medium term solution to climate change requirements.

At the same time, the climate agenda was growing in importance in the international context and, despite the Bank's efforts, the EBRD region continued, on the whole, to be highly energy intensive and inefficient. An effort to maintain momentum was still needed, especially as just before the financial crisis, at COP13 in 2007, the Bali Road Map had set a two-year timeframe to settle binding commitments on emission reductions ahead of the 2009 COP15 in Copenhagen.

Energy security also remained of strategic importance to many EBRD countries and had grown in importance since the start of the SEI with serious gas supply interruptions in the region in 2006 and early 2009, and price increases exerted further pressures.

Conceptual considerations

The first stage of the SEI had made use of a conceptual framework which advocated that a portfolio of measures and policies be adopted to deal with global carbon emissions.[21] This view had supported a range of measures under the SEI from energy efficiency to renewables, fuel switching, biofuels and tariff changes.

As the EBRD began thinking about a second phase for the initiative, a McKinsey report prepared with the Vattenfall Institute of Economic Research, provided a precise way to assess different interventions and measure the abatement costs of per ton of avoided emissions.[22]

Many of the areas being addressed by SEI activities involved a negative cost, particularly those relating to improved energy efficiency. Industrial and power sector projects and renewables were also at the lower end of the cost scale helping to vindicate the SEI approach.

---

21 Using the notion of stabilisation wedges (the difference between a 'business as usual' path and a stabilisation/flat emissions path), Professors Pacala and Socolow of Princeton University identified 15 actions that could stabilise emissions by 2054, including in the areas of energy efficiency and conservation, fuel shift, nuclear and renewables which the Bank could readily pursue. (Others were carbon capture and storage, forests and agricultural soil conservation.) S. Pacala and R. Socolow, 'Stabilisation Wedges: Solving the Climate Problem for the Next 50 Years with Current Technologies', *Science*, vol. 305, 5686, 13 August 2004, pp. 968–972.

22 'Pathways to a Low-Carbon Economy', McKinsey & Company, 2007. The report was updated in 2009, see https://www.mckinsey.com/~/media/mckinsey/dotcom/client_service/sustainability/cost%20curve%20pdfs/pathways_lowcarbon_economy_version2.ashx.

As well as arguing that energy efficiency was a cost-effective way of tackling climate change, along with decarbonising energy sources and adopting new low carbon technologies, McKinsey advocated changing the behaviours of businesses and consumers. This fitted well with the Bank's transition approach. Among other operations, the SEFFs were a key tool in this regard.

SEI Phase 2

After taking account of the McKinsey findings, the second stage of the SEI continued to focus on energy efficiency and renewables but proposed to add buildings, biomass (given the extent of forestry and agricultural waste products in the region), increased attention to gas flaring, transport (which had grown quickly, shifting away from rail), and adaptation to the list of targeted areas. Standalone corporate sector projects focused on the most energy intensive industries with assessments made during site visits by the E2C2 team providing the basis for specific components.

Donor-funded energy audits leading to rational energy use programmes were incorporated into long-term investment plans. One aim was to introduce best practices and improvements to the energy management methods of clients. Similarly, SEFFs with inbuilt technical, economic and awareness-raising components, helped motivate consumers to seek more rational use of energy.

Technical assistance via selected consultants helped to raise awareness among borrowers of the financial attractiveness of sustainable energy investments.

The importance of the SEI to the Bank's strategy was reinforced by the Board of Governors at the 2009 Annual Meeting, where they unanimously agreed to make energy efficiency and climate change a full component of the medium-term transition agenda.[23] The following year's Annual Meeting in Zagreb endorsed the approach and made it one of five core areas of Bank activity for the planning period 2011-2015 under CRR4.[24]

However, it was not all plain sailing. Three underlying issues had raised anxieties among some observers and needed attention. These were the extent

---

23 'Fighting the Crisis, Promoting Recovery and Deepening Transition', April 2009.

24 'Capital Resources Review 4', 29 March 2010. The other priority areas were: building stable financial sectors; diversifying economies; accelerating transition in infrastructure; and applying the lessons of the crisis.

to which the initiative might be driven by a desire for business volume rather than targets for carbon savings or improvements in climate resilience and measurement of these outcomes; questions over the use of subsidies; and the extent to which the initiative—which under Phase 2 proposed a more than doubling of the volume target to €3 billion to €5 billion—conformed with the original transition mandate of the Bank.

6. Carbon Reduction Targets?

The value of signed investment volume was a key motivation for Bank staff since it fed into their personal performance objectives. It was also clear from the corporate perspective that business volume, and its scaling up, was integral to the Bank's performance but also to the delivery of projects and policy interventions needed for sustainable energy solutions in countries of operations.

The issue of how to measure success was raised by the Evaluation Department. In its assessment of the SEI[25] it had argued that more attention needed to be paid to the extent of greenhouse gas reductions—since this was a primary goal of the initiative—than to the volume of business activity.

Banking disagreed with the idea that carbon reduction was being sacrificed for investment volume. In many cases, projects came about as a result of opportunities to cut emissions and the involvement of the E2C2 team—who had their own perspectives, objectives and targets. Furthermore, many projects had a wider impact through raising awareness of energy efficiency. A better understanding of the impact of the initiative on climate change made sense nonetheless, so CO_2 reduction targets were included in the second phase of the SEI. These were achieved, albeit at the lower end of the scale.[26]

The debate over the measurement of emission reductions continued. One problem was that the target measured expected reductions of CO_2 rather than outcomes. The Evaluation Department noted that insufficient

25 'Special Study on the Sustainable Energy Initiative Phase I Strategic Review', October 2010.

26 The influence of the earlier Evaluation Report was acknowledged in the Board paper on the SEI Phase 3: "The Bank's ability to report SEI results has improved during SEI 2 … [as] a response to the Bank's Evaluation Department review of SEI Phase 1 … At the same time, the Bank seeks to strike the right balance between the development of new activity with increased attention to monitoring." 'Sustainable Energy Initiative Phase 3', 1 March 2012.

attention was paid to collecting relevant information (or articulating counterfactuals) that would help the Bank reach more definitive conclusions on the results of its interventions. This limitation reflected resource constraints both within the Bank and for clients, particularly for projects requiring significant analysis for the precise assessment of outcomes.

It might have seemed logical from a climate perspective to simply target direct GHG reductions. But it was not altogether practical and there were measurement and other problems whichever way the issue was looked at. For example, GHG savings per unit of investment were six to seven times larger in natural resource projects than their nearest rivals in power and energy, yet it clearly did not make sense to shift Bank resources heavily into natural resources. Similarly, a transformative project demonstrating the value of a new technological advance or a major policy change could have significant indirect effects on GHG reduction, for example grid modernisation which integrated renewable energy into the electricity system. The unpredictability of demand for investment (particularly post-crisis) and its carbon saving potential, geographical and sectoral spread were further arguments for caution.[27]

There were in any case wider objectives than GHG reductions, such as systemic change, policy improvements and capacity-building, which had to be considered. More generally, climate change experts gradually moved away from GHG emission reduction assessments at a project or facility level in favour of alignment of facilities with COP goals.

Scorecard targets became focused instead on the share of SEI business in the Bank's total, starting with an objective of 23 per cent for 2011 (and 25 per cent for 2012). This was in part justified by the idea of mainstreaming climate change activities.

The debate on the measurement of interventions to mitigate climate change was not confined to the EBRD. The World Bank and other MDBs struggled to find the right metrics to measure the results of investments and policy changes focused on climate change. The EBRD was at the forefront

27 Increased attention to buildings or greenfield rather than modernisation projects tended to have lower carbon reduction effects, for example, as did a switch away from retrofitting fossil fuel plants. Municipal projects with a high share of EBRD financing compared with industrial projects with a large share of financing syndicated to multiple lenders also altered the GHG reduction per unit of EBRD finance equation. As did limitations on investments in energy-intensive, state-owned enterprises that were not slated for privatisation.

of thinking about climate finance accounting as a result of the efforts it was making on climate-related activities.

A further spur came from donors who, like the EBRD's shareholders, wanted to explain to their trustees, supporters and the public the impact their finance was having in mitigating global emissions. Here, the Bank's experience in building methodologies for tracking GHG emission reduction results, from operating two carbon funds under Kyoto and Green Investment Schemes (GIS) in Poland and Slovakia, was important. It led to the development of a Monitoring, Reporting and Verification (MRV) system to track results and a more accurate estimate of the impact of the Bank's operations.

The MRV system identified the environmental component of each project and the relevant amount of finance involved on a consistent basis and set a baseline scenario from which to measure the impact of the project after implementation and then report the actual impact. The system was linked to a dedicated project management information system to track the overall impact of the EBRD's green activities, including carbon emissions reduction, energy and water savings, renewable energy production and other elements. By providing detailed information to individual banking teams, it supported their results management and performance targeting. The system also provided information that allowed the EBRD to contribute to the first annual joint MDB climate finance report (published in 2012 showing results for 2011), based on common standards and reporting practices which the Bank helped design, working closely with the other MDBs.[28]

7. The Use of Grants and Subsidies

In the effort to address market failures and scale up climate-related activity, the use of technical cooperation, investment grants and concessional funds had grown quickly. Cumulatively investment grants trebled from a low base between SEI Phase 1 and Phase 2.

---

28 The MDBs jointly operate (with rotating chairmanship) a climate management group which meets at the IMF/World Bank Annual Meetings. Initially involving the African Development Bank, Asian Development Bank, EBRD, EIB, Inter-American Development Bank and the World Bank Group, it expanded to include the Asian Infrastructure Investment Bank, Islamic Development Bank and the New Development Bank. In 2019, MDB climate financing by the original members had reached US$ 61.6 billion. See the 2019 Joint Report on Multilateral Development Banks' Climate Finance, prepared by the EBRD and published in August 2020, www.ebrd.com.

Ordinarily for an MDB, the use of grants would have been little questioned—and indeed many funds for climate change purposes were designed to provide subsidised finance to assist poorer countries. But with the EBRD focusing on the private sector and investing in several upper middle-income countries, the role and use of below-market finance and subsidies was a legitimate concern.

The two uses of these funds served different purposes. One part covered technical assistance for items like energy audits, feasibility studies, project preparation, product promotion, monitoring and energy and social action plans.[29] This helped to improve the quality of projects and support clients in identifying and developing the energy efficiency opportunity and ensured they complied with the Bank's environmental and social standards.

Although some critics argued that they were used as a sweetener for projects, these funds helped improve client understanding and overcome inertia. For projects under implementation, they helped the client to fulfil the Bank's onerous reporting and legal requirements.

Investment grants and concessional co-finance on the other hand, which were direct subsidies alongside EBRD finance, needed clearer justification. Strict adherence to the Bank's additionality principle meant that it was important to avoid undercutting the market through the use of subsidies. For the most part, competitive market finance was not available for the types of projects considered by the Bank, particularly taking account of the significant market distortions in areas covered by the SEI including the lack of a carbon price and, even worse, subsidies for fossil fuels.

Concessionality needed to be justified by the nature and degree of the market failure or externality being addressed. Here, for example, information asymmetries played a part in justifying incentive payments under SEFFs, while 'first mover' explanations could apply to new or innovative technologies. Affordability of basic services for poorer households was also cited as a reason in municipal cases where cost recovery or higher environmental standards raised prices.

---

29 Among the heaviest users of these types of funds were environmental improvement projects with municipalities. Often located in less populated or remote regions of countries, the lack of understanding of western norms were fundamental barriers that needed to be overcome. Consultants employed to improve regulatory practices frequently had to overcome resistance arising from lengthy and complex political decision-making processes.

Several Board Directors represented donors as well as national finance departments. While they were keen for donor funds to be used for purposes like climate change mitigation they wanted reassurance that they represented good value for money. The creation of the Special Shareholders' Fund (SSF)[30] in 2008, which was used to support the energy efficiency and climate change agenda, further supported the pursuit of this goal. To provide a check on proper use of the SSF, OCE had prepared a set of Guidelines on the use of investment grants which became more relevant as the use of concessional funds grew.[31]

Guidelines on concessional finance

The Guidelines, which were updated a few years later to cover all concessional finance instruments used by the Bank,[32] were couched in terms of the Bank's approach towards transition and additionality. Improperly used, grants had the potential to distort market signals and lead to an inefficient allocation of resources. On the other hand, their selective use could redress market failures and social deprivation arising from the adoption of market practices and prices.

The Guidelines focused on key principles that needed to be verified for concessionality to be acceptable: market subsidiarity (where objectives could not be achieved with market instruments alone), leverage for systemic change, economic viability and longer run sustainability (once barriers were overcome), and minimum concessionality (only using the amount necessary to meet the objective).

The Guidelines spelled out how grants should be applied for environmental infrastructure investments, sustainable energy and resource efficiency projects and financial intermediaries. There was some debate with the Board whether financial incentives should be offered to commercial banks, since some Directors believed this might undermine market principles and

30 See Kilpatrick, *After the Berlin Wall,* Chapter 12, pp. 349-50.

31 'Staff Guidelines for the Use of Non-TC Grants from the Shareholder Special Fund', 7 April 2008.

32 Concessional finance typically refers to the use of investment grants, interest rate subsidies and guarantees such as risk sharing and first loss cover. Following a Grant Co-financing Strategic Review in 2013, an updated, more detailed and practical version of the Guidelines was issued, designed to improve the governance of concessional finance and extend the use of the Guidelines across all sources of Bank-managed donor resources. 'Staff Guidelines for the Use of Non-TC Grants in EBRD Operations', 15 January 2015. These were updated further as 'Staff Guidelines for the Use of Concessional Finance Products in EBRD Operations', 21 June 2017.

lead to demands for subsidies for other credit lines. Management argued successfully that market lending for energy efficiency was undersupplied as a result of first mover externalities[33] and that monitoring technical details, where the wider public interest diverged from that of the financial institution, needed support.

More broadly and regardless of sector, investment grants were expected to show an underlying economic justification, efficiency in design, relevance in the context of the policy environment and how they represented a priority use of scarce donor funds.

The Guidelines also provided a basis for the EBRD's input into work by DFIs to reach agreement on principles and definitions on concessional finance. Under the leadership of the EBRD and the IFC, a working group of MDBs (and bilateral agencies) produced a paper for the Heads of MDBs meeting in Washington in April 2013, which they endorsed, setting out DFI Guidance for the use of concessional finance in private sector operations.[34] This was later supplemented with a similar set of principles for the use of blended concessional finance among DFIs, where again the EBRD played an important role.[35]

Donor views

From a donor perspective, the EBRD provided a strong vehicle for the deployment of climate funds to poorer and highly energy inefficient countries, especially in eastern Europe, the Caucasus and Central Asia and, later on, in North Africa. Initially, the main contributions were from bilateral donors and the EU, mostly for energy efficiency audits and incentives under SEFFs. The SEI concessional funding strategy also included multilateral funds reflecting the scale and urgency of the climate change problem.

Building on its early experience with the SEI, the EBRD contributed actively to the concept and development of the multi-donor Climate Investment Funds (CIFs). Following its establishment, the Bank became an

33 Where new forms of lending or to a new client base involved significant risks, for example due to a lack of experience (as with energy efficiency) and client track records.

34 'DFI Guidance for Using Investment Concessional Finance in Private Sector Operations', 15 April 2013, https://www.ebrd.com/downloads/news/roundtable.pdf.

35 'DFI Working Group on Blended Concessional Finance for Private Sector Projects', Joint Report, October 2019 Update, EBRD, EIB, IFC, other MDBs and DFIs.

implementing agency and a first EBRD Climate Investment Special Fund was established in October 2009. In this manner, the Bank was able to contribute alongside other MDBs to the development of the global climate finance architecture, while gaining access to large donor contributions to support market transformation at a greater scale.

The Bank's success in deploying these funds led to an extension of the approach through the use of major funds such as the Global Environment Facility (GEF), the Special Climate Change Fund (SCCF), which focused on adaptation, and through funds created under the Eastern Europe Energy Efficiency and Environment Partnership (E5P), a multi-donor fund modelled on the Northern Dimension Environmental Partnership (NDEP),[36] covering Armenia, Azerbaijan, Belarus, Georgia, Moldova and Ukraine. As an implementing agency for these funds, the Bank received dedicated budgets and earned management fees (mainly from the CIF and GEF) and this helped to strengthen its capacity to further scale-up climate finance.

8. Climate Change and Transition

The increased focus on sustainable energy and its rising share in the EBRD's annual investment volume led some Directors to question whether in pursuing climate change goals the Bank was straying from its original mandate.

A series of papers discussed by the Board between 2008 and 2012 helped to embed the view that a low carbon pathway was consistent with transition towards a market-oriented and sustainable economic system.

Given its past treatment in command economies, there was no dispute that the promotion of environmentally sound and sustainable development

36 See Kilpatrick, *After the Berlin Wall,* Chapter 8, pp. 240–2. In 2009, during the Swedish presidency of the European Union, the E5P was created to encourage municipal investments in energy efficiency and environmental projects in the Eastern Partnership (EaP) region. The Fund tried to replicate the success of the NDEP in Russia and Belarus. By the end of 2020, 26 donors and eight MDBs had mobilised over €240 million for 41 projects for a total project value of €1.2 billion. Projects range from district heating, building energy efficiency to water and wastewater infrastructure, urban transport, street lighting and solid waste management. More than 1 million tonnes of CO_2e and 815 GWh per annum are expected to be saved every year, with multiple other societal benefits in terms of gender, employment and economic growth. It is estimated that the impact of E5P projects have directly benefitted or will benefit 12 million people, or 16 per cent of the EaP population. Additionally, the Fund has served as a platform to discuss regulatory changes and promote project-specific policy reform, thus indirectly benefiting a much larger number of people. In November 2019, during the 10th anniversary of the EaP, the Fund was successfully extended and replenished for 10 more years.

went hand-in-hand with other aspects of the transition process. But, as described in Chapter 6, environmental considerations had been somewhat downplayed, so a closer integration of environmental activities with the transition impact assessment system was introduced over this period.[37] Greater recognition was also given to the view that a critical mass of projects could leverage policy and institutional change and that large numbers of small projects could generate overall demonstration effects, as in SEFFs.

The Board became persuaded that climate change and energy efficiency could be brought more effectively into the existing system of project appraisal. Like other aspects of transition, the shift towards an energy efficient and low carbon economy focused on the transformation of markets, behaviours, products and processes and deployment of new skills; and a sound institutional, legal and regulatory framework was required to stimulate investment, create the right incentives and overcome market failures. They agreed with management that sustainable energy efforts were best promoted through a combination of investments, institutional reforms and policy dialogue.

9. Copenhagen COP15

As the second stage of the SEI got underway, international climate negotiations were intensifying with a view to a global agreement at COP15 in Copenhagen in December 2009. The IPCC fourth report, published in late 2007, had made clear that "warming of the climate system is unequivocal."[38] At the time, there was broad scientific agreement that global emissions would need to fall by between 50 and 85 per cent of 2000 levels by 2050, in order to restrict global warming to less than 2.5 degrees centigrade.

COP15 was supposed to reach a global agreement but in spite of all-night efforts by heads of state and negotiators, the meeting failed to deliver a legally binding agreement. Despite the different views over the speed of action needed to address climate change the Copenhagen Accord—which for the first time included the two largest global emitters, the USA and China, making commitments on emission reductions—managed to agree that:

---

37 These developments are described in Chapter 6.

38 IPCC, 2007: Climate Change 2007: Synthesis Report. Contribution of Working Groups I, II and III to the Fourth Assessment Report of the Intergovernmental Panel on Climate Change, Core Writing Team, Pachauri, R.K and Reisinger, A. (eds.), IPCC, Geneva, p. 104.

> Scaled up, new and additional, predictable and adequate funding as well as improved access shall be provided to developing countries … to enable and support enhanced action on climate mitigation …

And that developed countries would commit new and additional resources:

> … approaching US$ 30 billion for the period 2010-2012 with balanced allocation between adaptation and mitigation …[and] to a goal of mobilizing jointly US$ 100 billion a year by 2020 to address the needs of developing countries. This funding will come from a wide variety of sources, public and private, bilateral and multilateral, including alternative sources of finance.[39]

A High-Level Advisory Group on Climate Financing (AGF) was established shortly afterwards by Ban Ki-moon, the UN Secretary General, to help identify sources of finance, as requested by the COP. The AGF was co-chaired by Prime Ministers Jens Stoltenberg of Norway and Meles Zanawi of Ethiopia, and the EBRD contributed directly to several workstreams of the Group, notably those on private sector and MDB finance where it coordinated inputs from the ADB, AfDB, EIB, IADB, World Bank, IFC and others.[40]

The EBRD's experience was valued for its strong operational record of delivery, leveraging of private finance, innovative financing instruments and energy efficiency focus. Financial arrangements under the AGF were formalised at the following year's COP in Cancun, which saw the Green Climate Fund (GCF) announced and further financing targets agreed towards mobilising US$ 100 billion per year to assist developing countries by 2020.

The global effort to focus more concretely on climate change financing was welcome news and supported the Bank's efforts. Nonetheless, one important area of potential leverage, the carbon market, was not developing as well as hoped. The recession had undermined the relatively immature and fragmented market system and carbon prices were volatile and weak. In particular, lower industrial activity resulted in a collapse of carbon prices.

---

39 Report of the Conference of Parties of Decisions Adopted, Decision 2, the 'Copenhagen Accord', para. 8, 18 December 2009. UNFCCC/CP/2009/11/Add.1. https://unfccc.int/sites/default/files/resource/docs/2009/cop15/eng/11a01.pdf.

40 'Sustainable Energy Initiative', Information Session, 8 February 2011.

A consequence of this outcome was that national policies, such as higher standards and externality-correcting taxes and subsidies, and international public finance flows including support from multi-donor joint-MDB funds, seemed more likely to be the drivers of climate mitigation actions in the short to medium term rather than carbon price signals.

The urgency of action needed, further emphasised in December 2009 by Stern[41] who suggested the target to limit the global average temperature change to 2 degrees Celsius was at risk despite the Copenhagen Accord, gave impetus to the EBRD corporate team's view that it was important to accelerate and scale up climate change mitigation investments and measures to reduce the risks identified by Stern and others.

10. From SEI to SRI

Following Copenhagen, the second phase of the SEI, which was generating a strong momentum within the Bank, scaled up its business. A particularly valuable impetus came from the role of SEFFs whose volume began to accelerate, helped by a significant appetite for on-lending for energy efficiency and renewables' projects by large banks in Turkey, a recent addition to the EBRD's list of countries of operations. (See Box, Sustainable Energy Financing Facilities: The SEFF Model, p. 368.)

Under the second phase of the SEI, closer attention was paid to the calibration of subsidies. The idea of 'smart' non-distortionary subsidies was introduced to address barriers to energy efficiency and accelerate the dissemination of information and demonstration effects. This time CO_2 reduction targets were set, of 25 to 35 million tonnes CO_2 per year, making the EBRD the only international financial institution to have a formal CO_2 mitigation target.

Despite the difficult economic conditions following the financial crisis, the targets were exceeded, with EBRD financing reaching more than €6 billion for almost 300 operations and a total project value of around

41 LSE Press release, 19 December 2009. 'It is disappointing that the Copenhagen climate change conference has not succeeded in producing a political agreement that has been signed by all countries. ... Current intentions fall short of the 2020 target of 44 billion tonnes by several billion tonnes. Countries must come forward now with strong commitments to ensure the world is on an emissions pathway that is consistent with the 2 degrees goal', N. Stern 'Statement from Copenhagen'

€33 billion, with two-thirds of investments in the private sector. Between 2009 and 2011, annual SEI investments doubled from €1.3 billion to €2.6 billion and carbon emission reductions was estimated at almost 26 million tonnes of CO_2 per year.

Donor funds also increased above expectations, spurred on by a range of facilities operated by the EU.[42] Several climate investment funds provided through multilateral sources were used, including the Climate Technology Fund (CTF), the GEF and the new E5P focused on Ukraine and other countries of the Eastern Partnership. Encouragingly, a number of advanced transition countries also became donors.[43]

Management soon began thinking about a Phase 3 for the initiative, to run from 2012 to 2014.

The Sustainable Resource Initiative (SRI)

The SEI Phase 3 was introduced in March 2012.[44] During consultations leading up to it, attention was drawn to the broader question of resource efficiency beyond energy. Stakeholders saw resource use as strategically relevant to the Bank's environmental agenda. Operational experience acquired through implementation of the SEI suggested there was scope to expand the initiative into two additional areas, covering water and materials efficiency.

One of the Task Forces set up after Suma Chakrabarti's arrival as President that summer, on Sector and Product Innovation, recommended in November 2012[45] that the Bank should establish a Sustainable Resource Initiative (SRI). The parallel Task Force on the Results Framework agreed with the idea concluding: "… there is no question that helping countries of operations to build economic systems which deal with resources efficiently is part of the EBRD's transition mandate".[46]

---

42 Facilities such as the Bohunice International Decommissioning Support Fund (BIDSF), Instrument for Pre-Accession Assistance (IPA), Kozloduy International Decommissioning Support Fund (KIDSF) and Neighbourhood Investment Facility (NIF).

43 Czech Republic, Hungary, Poland, Slovakia, and Slovenia. South Korea also became a bilateral donor to climate objectives during this time.

44 'Sustainable Energy Initiative Phase 3, 2012–2014', 1 March 2012.

45 The 'Report of the Sector and Product Task Force' to the Executive Committee, 15 November 2012. See also a presentation to the Board, 'Sector and Product Innovation', 29 January 2013.

46 'Results Framework Task Force', 2012.

Sustainable Energy Financing Facilities: The SEFF Model

The SEFF model was based on the EBRD extending credit lines to local financial institutions that sought to develop sustainable energy financing as a permanent area of business. Finance for sustainable energy projects was provided specifically for energy efficiency and small-scale renewable energy projects. The aim was to build a model under which financial institutions, leasing companies and microfinance institutions would appreciate the value of offering clients opportunities to introduce cost-saving energy efficient technologies and become comfortable with the risks and procedures in doing so. This would have demonstration effects in the market leading eventually to a diminishing need for EBRD and donor financial support while promoting climate-friendly investments.

Local financial institutions on-lent the EBRD funds to their clients: small and medium-sized businesses, corporate and residential borrowers, and renewable energy project developers. SEFF Project Implementation Teams, made up of local and international experts, provided support to the local banks and their clients. They trained staff on how to promote the new financial product and how to recognise and originate eligible financing opportunities. The experts also provided borrowers with support in identifying energy saving opportunities, developing financing applications, enhancing project design, and advising on high performance technologies.

SEFF financing for businesses typically ranged from a few hundred thousand to a few million euros to support the purchase and installation of equipment, systems or processes. It reached right across the whole range of economic sectors, ranging from agribusiness, food processing, and manufacturing to industry, construction and services. SEFF residential loans covered a few thousand to a few hundred thousand euros, most often to support environmentally sound building improvements. Beneficiaries included individual households, groups of home owners and multi-apartment building associations.

The EBRD also worked closely with donors to finance indispensable technical support and investment support to overcome perceived risk barriers and affordability constraints.

After a successful first test of the model in Bulgaria between 2004 and 2006 (see pp. 342–44), SEFFs were extended to a wide range of countries, 28 in all by 2020. Once Turkey became a country of operations in 2008, the scale of SEFF financing rose sharply as Turkish banks found significant demand for energy saving solutions among small Turkish businesses. TurSEFF, a facility of US$ 200 million and MidSEFF, a similar €400 million arrangement in Turkey targeting mid-sized corporates, both launched in 2010 under SEI phase 2, were significant additions to the armoury. High demand meant that both facilities were later extended twice, together with co-financing partners, to reach a total of €2.5 billion.

With the advent of the GET in 2015 and its wider scope than the SEI, SEFFs shifted to Green Economy Financing Facilities (GEFFs) in 2017, to reflect additional objectives beyond energy such as resource savings. The model however remained the same.

By 2020, the SEFFs and GEFFs portfolio was almost €5 billion and the facilities had contributed approximately 15 per cent of the volume under the Bank's green finance initiatives.

Resource efficiency had been gaining international recognition since the G8 Sea Island Summit in Georgia, USA in 2004, where leaders committed to a 'Reduce, Reuse, and Recycle (3R) Initiative' the following year. At the 2008 G8 Environment Ministers' meeting in Kobe, Japan, a 3R Action Plan was introduced in what was described as a "… spirit of *mottainai*[47] [to] prioritize actions to curb unsustainable consumption of natural resources … [and] give high priority to waste reduction."[48] The Plan also called on bilateral and multilateral aid agencies to "… reflect the concept of the 3Rs in development projects and that private investors promote 3Rs in developing countries".

---

47 The Action Plan explained further that "*mottainai* is a long-established Japanese concept meaning that it is a shame for something to go to waste without having made use of its potential in full. This expression incorporates a respect for the environment that has been handed down from ages past." p.3.

48 Kobe 3R Action Plan, 24-26 May 2008, Government of Japan, https://www.env.go.jp/en/focus/attach/080610-a5.pdf.

In September 2011, the European Commission put forward a 'Roadmap to a Resource-Efficient Europe'[49] along with a number of Directives (and thus directly relevant to some EBRD countries), as part of the EU's Europe 2020 strategy.

Although global efforts on resources appeared less important to the needs of the EBRD region compared with energy efficiency they were not irrelevant. For example, Central Asia had seen disputes over many years in the Ferghana Valley over water use between Tajikistan and the Kyrgyz Republic and downstream Uzbekistan (also Kazakhstan); improved energy efficiency would also ease pressures to divert water to generate hydroelectric power.

However, it was the arrival of new EBRD countries of operations in MENA in 2012 that helped sharpen the focus on the role the Bank might play in tackling the inefficient use of water resources. Furthermore, the UN Summit on Sustainable Development in Rio in 2012 (the 'Rio+20' Earth Summit) placed a focus on the conservation of resources as it started work to replace the Millennium Development Goals (MDGs) with the Sustainable Development Goals (SDGs).

The SEI Phase 3 had been put forward a little ahead of the Rio Earth Summit that June. Management then saw the SRI as an opportunity to create an umbrella initiative consistent with international developments, by keeping the existing SEI as its core component but extending the initiative to new water efficiency and materials efficiency areas. On that basis, the SRI was launched at the Governors' Annual Meeting in Istanbul in May 2013.[50]

While the SRI was widely accepted and endorsed by Governors, it had not been without a few debates. Directors had again raised the issue of consistency with the Bank's mandate but also what it might mean in practice. Some railed against expanding the scope suggesting the Bank was moving in too many directions (they were still adjusting to the increased attention to sustainable energy). Management responded by emphasising their efforts would maintain a bottom-up approach, driven by client demand and that it did not imply a new development agenda.

---

49 'Roadmap to a Resource Efficient Europe', COM (2011) 571 (Final), 20 September 2011, Communication from the European Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, Brussels.

50 2013 also happened to be the UN International Year of Water Cooperation.

The practical question was mainly about allocation of Bank resources, where some worried a further initiative would complicate project selection. They queried whether projects involving water use would be bankable. Many pointed out other IFIs already had significant programmes in place covering water resources.

In the end it was accepted that there was complementarity in the SRI with the Bank's mandate, business model and its operations, particularly in territories where water scarcity was a major problem. It also helped that it fitted with the EU's resource agenda.

The SRI design was similar to the SEI except that it now included a focus on the efficient management of water and materials. The idea was to add these elements as part of an enhanced product offer to clients alongside the energy efficiency work. In some cases, there were synergies to be exploited, for example where audits could consider water and materials' use as well as energy consumption. But when it was introduced a lot remained to be worked out. Furthermore, the economists objected to the materials dimension arguing that normal market processes would lead to the efficient use of inputs, including materials, so that something beyond the norm was needed to be counted as genuine progress.

In substance, the SRI did not result in a major shift away from the SEI activities as it remained dominated by energy efficiency and climate change operations. Nonetheless, in 2013 and 2014, water and materials efficiency project volume reached around €800 million for around 70 projects, mainly related to water management or around 15 per cent of the SRI total. Although physical targets had not been set, the MRV system in operation by 2015 showed (by mid-June 2015) over 10 million cubic metres of water per annum and nearly 400,000 tons of waste per year avoided.

Some innovative waste projects were introduced, such as a major glass recycling project with Şişecam in Turkey.[51] And the SRI achieved a step up in climate adaptation finance which reached over 5 per cent of the annual total by the end of 2014.

---

51 This project triggered the Near Zero Waste (NØW) Progamme, recognised by the CIF as a success: https://www.climateinvestmentfunds.org/cif_enc/news/near-zero-waste-turkey-moving-toward-circular-economy-monetizing-waste.

11. Green Economy Transition (GET) and COP21

While the SRI represented an incremental advance on the SEI, there was a desire to pull together the different strands involved in the climate work and integrate them more fully into the Bank's transition model which itself was under review in early 2015 (see Chapter 6).

Green financing already exceeded one quarter of EBRD annual business volume and the evidence showed it scored well in terms of operating margins and assessed transition impact. A further push along the low carbon transition path the Bank was pursuing made sense in the period ahead, and played into the next capital resources review covering the period 2016–2020 as it was being finalised ahead of the 2015 Tbilisi Annual Meeting.

A further key factor was the upcoming COP21 Paris Climate Summit scheduled for December, where the French hosts were seeking to reach a global climate agreement. The preceding major international events building up to the UN General Assembly in September and agreement on the SDGs, which included sustainable resource and energy goals, added impetus to the Bank's strategic directions on climate action.

The G7 summit declaration in June reaffirmed their commitment to decarbonisation and cuts in global GHG emissions and to the Copenhagen Accord's aim of mobilising climate finance of US$ 100 billion per year by 2020. Led by the German Chancellor, Angela Merkel, as President of the G7, leaders called on MDBs: "to use to the fullest extent possible their balance sheets and their capacity to mobilize other partners in support of country-led programs to meet this goal."[52]

French President Francois Hollande was keen to ensure success for the global climate summit in Paris later that year. A letter was sent by the Ministers of Finance of France and Peru (as host of that year's Annual IMF/World Bank meetings) in the summer, inviting the EBRD to "initiate a discussion with all shareholders on the possibility to enrich EBRD's current mandate with a specific 'transition towards green economy' strategic pillar … [which could lead] to forward-looking declarations and announcements ahead of COP21."[53]

52 Leaders' Declaration, G7 Summit, p.12, 7-8 June 2015, Schloss Elmau, Germany.
53 Quoted in 'Green Economy Transition Approach', October 2015, p. 5.

One of the opportunities to make a forward-looking announcement and build momentum ahead of COP21 was a meeting of Ministers of Finance organised by the French and Peruvian authorities in the margins of the Lima IMF/World Bank Group Annual Meetings in October.

The EBRD was in a good position to respond considering its green finance track record over the previous decade. But rather than put forward its most recent initiative, the SRI, at the Ministerial meeting, the Bank decided to give the EBRD's sustainability effort an even higher profile by seeking the Board's agreement to the Green Economy Transition (GET) approach.

The substance of the GET was broadly similar to the SRI but offered a stronger linkage to the transition concept embedded in the Bank's modus operandi—putting the case for pursuing a low carbon transition based on the careful application of market-supporting actions alongside debt and equity finance—and with the SDGs.[54] The EBRD would work with others, especially the private sector and other MDBs, in a joint effort to promote improved climate outcomes.

The Board was supportive but some nervousness was expressed again over the risk of decline of other core activities and, more strongly, over the stated intention that public sector projects could feature more prominently under this approach. Reassured by the analysis that the SEI/SRI was profitable and impactful, and had been successfully deployed widely across the activities of the Bank with a high private sector share, the Board unanimously endorsed the GET approach at their meeting on 30 September.

The timing of this approval a few days after the UN General Assembly meeting in New York and the adoption of the SDGs, and a little ahead of the Ministerial meeting in Lima, worked well. The President flew to Peru to present the GET approach and targets at the Climate Finance Ministerial meeting on 9 October.

Chakrabarti highlighted the EBRD's new commitment for up to €18 billion in GET financing and mobilisation of a further €60 billion for a total project value of €78 billion over its forthcoming strategy period. This represented a doubling of EBRD finance devoted to green activities to that point, which had involved 1,000 climate projects.

---

54 The GET was relevant to several SDGs: 6. Clean water and sanitation; 7. Affordable and Clean Energy; 8. Decent Work and Economic Growth; 9. Industry, Innovation, and Infrastructure; 12. Responsible Consumption and Production; and 13. Climate Action.

Under the GET approach, green economy finance was to increase its share of Bank business still further with the target set to reach 40 per cent of the EBRD's annual investment volume by 2020, up from the previous 25 per cent.

The presentation portrayed the seriousness with which the EBRD took climate finance. The intention that between a one-half and two-thirds of the green economy finance would be used to help the private sector invest in climate mitigation and adaptation projects put the Bank at the forefront of leveraging the private sector into climate action.

The GET envisaged further growth to meet demand for investment in areas such as renewable energy in the power and industrial sectors and for municipal district heating; energy and resource efficiency across sectors, including residential and commercial buildings; and solar energy in the southern and eastern Mediterranean to support a higher share of private sector power generation. A particular focus was on developing adaptation financing activity and accelerating the deployment of innovative technologies such as irrigation water efficiency and the development of bioenergy.

In a speech in Stockholm just ahead of the Paris Climate Summit, the EBRD's President summed up the Bank's position:

> A Green Economy is a market economy in which public and private investments are made with a specific concern to minimise the impact of economic activity on the environment. And where market failures are addressed through improved policy and legal frameworks aiming at accounting systematically for the inherent value of services provided by nature, managing related risks and catalysing innovation … the EBRD is today building on an established structure and model to deliver this scaling-up. While incremental resources and concessional funds will be needed, our operating model is ready and scalable.

Chakrabarti explained there was no longer a need to view "green" and "growth" as opposites or necessarily in competition with one another, but as complements:

> For many reasons, the debate is shifting. The technology driving green innovation is getting cheaper. Influential countries are rethinking where they stand on green investments. The market failures and barriers to change in climate finance are well known. … Our Green Economy Transition approach

> reflects … the economic rationale for green investments … [and] the scale and ambition of the EBRD's work to unlock new markets, introduce new technologies and support the growth of private sector environmental finance.[55]

12. The Paris Agreement

Paris, December 2015

On 12 December 2015, when French Foreign Minister Laurent Fabius banged down his gavel at the end of a 12-day international climate conference, there was a palpable sense of triumph. Close to 200 countries had just adopted the world's first legally binding international treaty on climate change.

The COP21 Paris meeting aimed to reduce the risks and impacts of climate change by limiting the average temperature rise in this century to well below 2 degrees Celsius, pursuing a more ambitious target of 1.5 degrees. The aim was to reach a global peak of greenhouse gas emissions as soon as possible and then reach for a climate neutral world by 2050. The countries that adopted the agreement would commit to taking concrete steps, their own individual carbon reduction targets or Nationally Determined Contributions (NDCs).

The path to the 2015 accord had been rocky and clouded by uncertainty right until the end. The last time the world had looked like getting to anything close to a similar deal had been at the COP15 talks in Copenhagen in 2009. Those discussions ended in disarray. This time it was different.

Clearly, there would be scepticism as to whether the goals could be achieved or whether they were ambitious enough. Eighteen months later, a newly-elected President Donald Trump would pull the USA out of the near universal agreement—only for his successor Joe Biden to sign up once again on the day of his inauguration in 2021.

But, at the time there was a genuine sense of achievement. Just hours after the pact was approved, US President Obama described it as "the best chance we have to save the one planet we've got".[56] World Bank President Jim

---

55 'Stepping up Green Financing', speech by President Chakrabati to the Swedish International Development Cooperation Agency, 13 November 2015, Stockholm, Sweden, https://www.ebrd.com/news/2015/stepping-up-green-financing.html

56 *Reuters*, 13 December 2015, 'Factbox: World reacts to new climate accord', https://www.reuters.com/article/us-climatechange-summit-reaction-factbox-idUSKBN0TV0Q420151213.

Yong Kim said the world had come together to forge a deal that reflected the aspiration to preserve the planet for future generations, proclaiming: "We called for strong ambition, for remarkable partnerships, for mobilization of finance, and for implementation of national climate plans. Paris delivered."[57]

EBRD President Chakrabarti called the Paris Accord a "major achievement" and said: "Now we face the challenge of turning the agreement into concrete steps. The EBRD is well equipped and willing to make a strong contribution." He noted that the EBRD's GET approach would ensure that combatting climate change and addressing its effects was integral to the Bank's activities.[58]

As the EBRD acted to integrate climate finance even more firmly within its operations, MDBs at the Paris conference signalled their intention to increase their collective impact. In a joint statement, the MDBs pledged to "increase our climate finance and to support the outcomes of the Paris conference through 2020 ... Each of our organisations has set goals for increasing its climate finance and for leveraging finance from other sources."

This commitment—from the AfDB, ADB, EBRD, EIB, IADB and the World Bank Group—supported the US$ 100 billion a year commitment by 2020 for climate action in developing countries that developed countries had called for in Copenhagen.[59]

The role of GET

The GET approach was the EBRD's own contribution to the new global drive to combat climate change. In addition to scaling up its operational and policy work to accelerate transition to low-carbon and climate resilient economies, the approach would broaden the environmental dimension of investments supported by the Bank. It aligned the way the Bank measured its contribution to the transformation of its economies—its transition impact rating—with the objectives of promoting a green economy. With the launch of the GET approach, the EBRD was placing the idea of tackling climate change even more firmly in the context of its own transition mandate.

57 Ibid.

58 EBRD Press release, 14 December 2015. 'EBRD committed to ensure implementation of historic Paris accord'.

59 EBRD Press release, 30 November 2015. 'Development banks vow to mobilise collective resources to confront climate change'.

The preamble to the GET proposals submitted to shareholders had quoted Stern:

> The risks of climate change are potentially immense. The benefits of taking action are also clear: we can see that economic development, reduced emissions, and creative adaptation go hand in hand. A committed and strong low-carbon transition could trigger a new wave of economic and technological transformation and investment, a new era of global and sustainable prosperity. Why, then, are we waiting?[60]

Stern reflected the EBRD's own logic—that transition to a low carbon economy was an essential element in the EBRD's mandate of delivering economic change.

Delivering Paris pledges

Virtually all the EBRD economies adopted the Paris Climate Agreement. Kosovo was unable to join the agreement because of its UN status, but it fully endorsed the Paris accord goals.

Turkey signed the agreement but by the end of 2020 it had still not ratified it, objecting to the fact that it had been classified among developed countries, obliging Ankara to provide financial resources to help developing countries achieve their Paris goals. That, however, did not stop Turkey setting ambitious green goals for its economy. In the wake of the Paris Agreement, green financing regularly accounted for around half of the EBRD's annual investments in the country.

The Bank quickly set to work helping its countries of operations deliver on the projects they planned as part of their national commitments. The EBRD's NDC Support Programme was set up specifically to help its countries develop, implement and strengthen their Paris commitments.

Early examples included Kazakhstan, where the EBRD had already helped with the development of country's INDC, its "intended" contribution, prepared in the run-up to Paris. After the Paris accord, the EBRD worked with the Kazakh authorities on carbon market and renewable

60 Nicholas Stern, *Why Are We Waiting? The Logic, Urgency and Promise of Tackling Climate Change* (Cambridge, MA: MIT Press, 2015).

energy policy issues linked to a renewable energy investment programme co-financed with the Green Climate Fund.

The Bank provided the Mongolian government with support in the development and implementation of finance tracking and monitoring tools and it conducted a policy/legal gap analysis for Morocco, Jordan and Tunisia in the SEMED region.

Climate adaptation and resilience measures

Some of the side events at the Paris climate conference had thrown a spotlight on the increasing devastation that global warming was inflicting on the planet. The Paris Agreement added momentum to the need for practical responses that supported climate change adaptation and helped scale up action to strengthen climate resilience.

Not many years earlier, the concept of climate adaptation had led to animated discussion within the EBRD. Some considered climate adaptation investment as an abdication of the responsibility for dealing with the root causes of global warming by just dealing with the symptoms. But the growing evidence of just how severely global warming was affecting agricultural sectors, the oceans and the threat to whole island states made it clear that there had to be a dual track approach.

The EBRD's climate resilience work did not start with Paris. In the four years to mid-2015, the Bank had invested €602 million on adaptation measures in 99 projects. But its activities moved up a gear as the Bank scaled up its green activities generally.

One of the countries in the EBRD regions most vulnerable to the impact of climate change was Tajikistan. The Central Asian economy was heavily dependent on rainfall and the melted mountain snow it needed for water and for electricity from its huge hydropower resources. Any changes in the amount of rain or available snowmelt had an immediate impact on the provision of water and energy, and on its agriculture.

In 2016, the EBRD introduced its CLIMADAPT climate adaptation programme in Tajikistan, working with international donors to provide loans to firms and private households to support the use of climate-resilient technology. The grant funding helped make the facilities more affordable and just one year later over 2,000 borrowers including private householders, farmers and small business owners had taken up loans to finance

technology for anything from irrigation to water storage, greenhouses and insulation.

The single standout climate adaptation investment in Tajikistan was the EBRD's financing package for the climate-resilient rehabilitation of the Qairokkum hydropower plant that helped improve the reliability of the country's electricity supply. The upgrade introduced innovative climate resilience measures that allowed the plant to cope with the impact of climate change on Tajik water and hydropower systems.

Four years later, the EBRD would issue the world's first ever bond dedicated specifically to funding climate resilience investments. The climate resilience bond was just one in a series of issues dedicated specifically to sustainable or green investments. The EBRD's first green bond had been launched in 2010. Ten years later, 94 Environmental Sustainability Bonds worth the equivalent of more than €5.2 billion had been issued, with 114 green bonds issued in all for a total of €7.3 billion.

By 2019, the EBRD had built up a portfolio of some €7 billion in climate resilient projects.

13. From SEFFs to GEFFs

SEFFs had proven effective at raising demand for sustainable energy projects via local banking systems. The new GET approach expanded the scope of the SEFF model to finance resource efficiency and climate resilience projects, in pursuit of increased transition impact.

In 2016, the world's largest dedicated fund helping developing countries reduce their greenhouse gas emissions and enhance their ability to respond to climate change—the Green Climate Fund (GCF)—approved its first large-scale project. The GCF-EBRD SEFF Co-financing Programme was worth US$ 378 million in grants and loans from the GCF and US$ 1.4 billion in total financing over 15 years. It remains the largest project approved by the GCF and provides support for climate change mitigation and adaptation investments in 10 of the most climate-vulnerable countries in the EBRD region.[61]

61 The 10 countries are Armenia, Egypt, Georgia, Jordan, Moldova, Mongolia, Morocco, Serbia, Tajikistan, and Tunisia.

"Working with the GCF requires meaningful engagement and endorsement at the country level," Ian Smith, an energy engineer and environmental economist who joined the Bank in 2007 to work on SEFFs, advises. "It is a great honour to have this backing, but also a significant responsibility to deliver on the climate commitments."[62]

Despite, or perhaps because of, the obvious success of the SEFFs, the EBRD decided to update the programme in 2017 at the time of an assessment of the progress of the GET approach. The SEFF was broadened out to better reflect the aims of the GET and, with the support of donor funding from Austria, was rebranded as GEFF, the Green Economy Financial Facility. The aim of the GEFF model was: "to transpose the EBRD Green Economy Transition approach into the operations of local financial institutions and their clients. The adoption of higher performance technologies, services and practices will ultimately transition the market to a green economy."[63]

Leander Treppel, EBRD Board Director for Austria, and long-standing supporter of SEFFs, said the GEFF was such an effective way to deliver GET and to influence the investment decisions of business and households that could not access EBRD support directly, that "if the model did not already exist, the Bank would have to create it".[64]

By 2017, the EBRD had been providing financing via the SEFFs for more than 10 years and supported over 112,000 investments across 24 countries, in association with more than 120 financial institutions. The EBRD provided financing of almost €4 billion, helping to avoid the equivalent of over 6 million tonnes CO_2 emissions a year.

"It took a lot of hard work from a lot of people to build a programme of this magnitude and keep it operational," explains Smith. "It really became a flagship product for the Bank with nothing else on the market able to deliver quite so effectively. When things got tough, we used to joke, 'If it was easy, anyone could do it!'"

The GEFFs built upon the strong operational experience of the SEFFs but they were designed to go further, helping to create green investment demand by informing clients of the business case for investing in higher performance technologies. It would increase awareness of the multiple benefits

62 Interview, 2021.
63 GET Implementation Update, 17 March 2017.
64 Statement at GEFF Launch in Kazakhstan.

associated with these technologies and demonstrate the cost-effectiveness of investing in green economy solutions for process modernisation, equipment upgrades and building refurbishment.

The Bank would also illustrate the business case for using commercial sources of finance to gain access to technology that had previously been deemed to be too expensive. It would partner with multiple financial institutions to instil competition and use their branch networks to increase geographic coverage and target a far greater number of beneficiaries than would otherwise be possible.

Despite the successes, the EBRD had observed that the uptake of higher performance technologies was being held back by obstacles, including a tendency of firms to avoid higher early mover costs by favouring smaller upfront expenses typically associated with lower performance technologies. As Smith observed:

> People kept buying technologies well below standard. When we demonstrated the financial benefits of the better technologies, we discovered that the barriers to uptake were not just restricted to being able to afford them; it was also about being able to find them.[65]

The GEFF model sought to change this pattern by establishing minimum performance criteria that made it easier for firms to identify and select higher performance technologies. In 2018, also with the support of donor funding from Austria, an on-line platform—the Green Technology Selector—was launched to showcase best-in-class technologies, covering everything from solar panels and biomass boilers to thermal insulation and heat pumps.

By 2020, the EBRD was working with over 150 local financial institutions in its region, across 27 countries. Around €5 billion of EBRD funds had now reached more than 200,000 green investments—a testament to the effectiveness of the Green Technology Selector—and together with funding from co-financing partners, GEFFs were now collectively avoiding almost 9 million tonnes of CO_2 emissions per year.

When asked about his favourite project, Smith recalls some of the more innovative technologies such as nano-filtration and sensors with artificial intelligence, but eventually settles on a piece of pipe. Smith explains:

---

65 Interview, 2021.

> A lady took a loan for a pipe to take water across her field, so the water didn't get lost through the irrigation channel and cause more soil erosion. This was a few hundred dollars' worth of micro finance. Within one season, the pipe and drip irrigation system allowed her land to become more fertile and she was able to get two crop rotations out of her field rather than one. Doubling her harvest easily allowed her to pay back the loan.

Sometimes the most modest of solutions can provide the best demonstration of impact.

14. Green Cities

One important area of green financing for the EBRD in the wake of the Paris Climate Accord and the launch of the GET approach was in urban sustainability—the greening of cities. There was clear potential for combatting global warming and climate change in urban areas. A report from the IEA in June 2016 showed that, while cities were home to about one-half of the global population, they represented almost two-thirds of global energy demand and 70 per cent of carbon emissions from the energy sector.[66]

After attending a major cities event at COP21 that gathered over 1,000 mayors from around the world, Tanaka, who had initiated the municipal and environmental infrastructure finance practice of the Bank, turned his attention to how it could scale-up green finance for cities. He came up with a specific approach as part of the GET which became the Green Cities Framework.

Following significant work involving both E2C2 and the infrastructure group, the Board approved in November 2016 a five-year, €250 million Green Cities Framework that aimed "to serve as a sector-wide catalyst for addressing environmental challenges at the City level".[67]

Under the new programme, the Bank would make environmentally friendly loans to municipalities, municipal-owned and private companies providing municipal services.

Crucially, the programme required early preparation of Green City

66 IEA Annual Report, Energy Technology Perspectives, 2016.
67 'Green Cities Framework', 30 November 2016.

Action Plans (GCAPs) which assessed the full range of environmental challenges the cities were facing. Lin O' Grady, a senior EBRD banker with over 20 years' experience in the transport and municipal infrastructure sectors, and Nigel Jollands, an EBRD climate and sustainable energy expert, teamed up to turn the Green Cities initiative into practical reality.

"It was pretty clear early on that by changing the way we interacted with cities we could really transform their green infrastructure investment process," said Jollands. According to O'Grady, "Green Cities completely changed the way we worked. Before that, we had just delivered individual municipal infrastructure projects—a waste management system here, or a fleet of new buses there."

Jollands added:

> With Green Cities, we began offering a joined-up approach by developing a green strategic vision—a Green City Action Plan—and linking that to investments. This was an attractive proposition for mayors who wanted to demonstrate their green credentials and deliver on the green promises they had made to their citizens.

The scheme also offered member cities the chance to join a group of cities pursuing similar goals and tackling similar urban challenges. It established a platform where experiences could be shared and lessons learnt from peers. "As we have discovered—cities like to network!" O'Grady said.

Each city that signed up to the programme joined the Green Cities Network and committed to develop a GCAP. The EBRD would simultaneously play its role as a financier, kicking off the process with a trigger investment. For O'Grady, this holistic approach made the crucial difference: "We were now talking to the municipal leaders, the mayors, about comprehensive programmes for the whole city, not just individual sub-segments. This level of access made the Bank's programmes far more visible and ultimately more effective."

Jollands also noted: "This approach resonated with Mayors—to such an extent that the Bank was able to attract business in cities where we had struggled to do business with before—I'm thinking about Batumi in Georgia and Sarajevo in Bosnia and Herzegovina to name just a couple."

O'Grady recalled her early meetings at the start of the Green Cities programme with Davit Narmania, the then Mayor of Tbilisi who had fought

his election campaign on a very strong green agenda. "We knew we were talking his language," O'Grady said. Narmania was very enthusiastic and Tbilisi became an early member of Green Cities in November 2016.

The first project under the Green Cities framework was approved just a month later in the Moldovan capital of Chișinău. This was a €10 million loan for energy efficiency in public buildings, co-financed with the EIB and supported by grant funding from the E5P. The financing package aimed to renovate 100 municipal buildings in Chișinău such as kindergartens, schools and hospitals which had considerable potential for energy efficiency savings, including from the introduction of rooftop solar projects.

The Green Cities programme took off with remarkable speed. An ambitious target of signing up 100 cities by 2024 was set which by the close of 2020 had already seen 45 cities join. The financial scale also rose significantly. The original €250 million was increased by another €700 million in 2018, with the addition of a significant contribution of €87 million from the GCF. That €950 million total doubled again in November 2020 to €1.9 billion, with very strong support from a number of bilateral donors.

Looking ahead, O'Grady said in January 2021 there were still gaps to fill. "We need to do more in Turkey," she said, noting that Ankara had just signed up in December 2020, only the second Turkish city after Izmir. In a vast country like Kazakhstan, the EBRD's programme was only present in Almaty and substantial possibilities remain in Egypt. Jollands also said more can be done:

> We are increasingly adding elements that make the programme even more effective. We are increasingly offering digital solutions that make for smart as well as green cities—like e-ticketing on buses or more sophisticated measurement for water consumption, and an e-learning platform for city officials to learn about how to implement climate action in their cities.

O'Grady was confident the 2024 target of 100 cities would be met. "This is a successful product that benefits from contributions from right across the Bank. It makes a difference."

15. The One Planet Summit

Two years to the day after the adoption of the Paris Agreement, Hollande's successor in the Elysée Palace, Emmanuel Macron hosted, together with Antonio Guterres, UN Secretary General, and World Bank President Jim Yong Kim, the first One Planet Summit that aimed to add more momentum to the Paris goals.

Behind the anniversary conference, lay one "obvious fact", the organisers said: "To achieve the objectives of the Paris Agreement, we must make stronger commitments, more concrete decisions and mobilize all stakeholders in public life and the economic world in collaborative efforts."[68]

Macron issued an urgent warning that the world was in danger of losing the battle against climate change. "We're not moving quickly enough. We all need to act," Macron told the conference.[69]

Earlier that year, Trump had formally signalled that the world's second largest carbon emitter would pull out of the Paris Agreement to which his predecessor had attached such significance.

Much of the rest of the world reacted with disappointment but little surprise. The French, German and Italian governments took the rare step of issuing a joint statement expressing their regret at the decision and their determination to press on with or without the Americans. The three leaders said:

> We are convinced that the implementation of the Paris Agreement offers substantial economic opportunities for prosperity and growth in our countries and on a global scale. We therefore reaffirm our strongest commitment to swiftly implement the Paris Agreement, including its climate finance goals and we encourage all our partners to speed up their action to combat climate change.[70]

The One Planet Summit was an opportunity for Chakrabarti to share with other political and development organisation leaders the progress that the EBRD was making in delivering on its new green targets. He told the

68 One Planet Summit Statement, 12 December 2017.

69 *Reuters*, 12 December 2017, 'France's Macron says world is losing battle against climate change', https://www.reuters.com/article/us-climatechange-summit-idUSKBN1E6217.

70 Statement on the United States of America's announcement to withdraw from the Paris Agreement on climate change, 1 June 2017.

conference that the Bank was set to achieve the target of dedicating 40 per cent of its annual investment by 2020 three years ahead of time. By the end of 2017, the Bank indeed exceeded the target three years ahead, with green investments accounting for 43 per cent of total EBRD investment.

At a side event at the Paris summit, major development institutions, including the EBRD, pledged to step up and deepen their cooperation in support of the Paris accord goals. In a spirit of collaboration, the institutions affirmed the "joint commitment to align their financial flows with the Paris Agreement".[71]

16. Renewables Revolution

The EBRD's renewables investments had overtaken financing for thermal power in 2014, even before the GET approach was unveiled in 2015. The Bank had invested €4.6 billion in renewable energy generation in the nine years since 2006. It was the largest investor in renewable sources of energy in its regions and had played a pioneering role in the sector, breaking new ground in the industry in several key countries.

Under GET, it pledged to do more. The GET approach put renewable energy development in the power and industrial sector as a top area to scale up its activity. The contribution from non-hydro renewable energy sources to the energy supply was still very low in most of the Bank's countries of operations.

The Bank saw particular potential in the southern and eastern Mediterranean, with its abundant natural resources of solar energy and at that point relatively low penetration of solar power plants. The EBRD would increase its investments, while at the same time working with authorities to realise their renewable ambitions and help some administrations overcome resistance to renewable energy.

A price revolution

There was at this time one global phenomenon that would propel the renewables activity of the Bank to new heights. The scale of renewable development and installation had reached a critical tipping point in terms of price.

71 EBRD Press release, 12 December 2017. 'Development groups step up collaboration to achieve Paris Agreement climate goals'.

In 2021, Harry Boyd-Carpenter was appointed Managing Director for Green Economy and Climate Action after several years in senior positions promoting investments and policy reform in sustainable energy at the EBRD.

Reflecting on the price trend, Boyd-Carpenter said: "This was the good news story that emerged in the five years since 2015. Renewables went through the floor in terms of price and through the roof in terms of deployment."[72] In 2010, said Boyd-Carpenter, the EBRD had been turning down solar projects because the price was too high: "Even five years ago, some projects were too expensive to do. Now they are too cheap not to do. No one expected this in 2015. It was a complete game changer."

Renewables such as solar and wind were becoming the dominant next phase in the industrial history of energy that had started with coal and moved through oil and then gas. The IEA concurred in its 2020 *World Energy Report*: "Solar PV is now consistently cheaper than new coal- or gas-fired power plants in most countries, and solar projects now offer some of the lowest cost electricity ever seen."

"I see solar becoming the new king of the world's electricity markets. Based on today's policy settings, it is on track to set new records for deployment every year after 2022," said Fatih Birol, the IEA Executive Director.[73]

A 2020 report from the International Renewable Energy Agency (IRENA) made clear that newly-installed renewable power capacity increasingly cost less than the cheapest power generation options based on fossil fuels. The ten years to 2019 had seen the sharpest fall in prices in solar photovoltaics (PV), where there had been an 82 per cent reduction, while prices for concentrated solar power were down 47 per cent, onshore wind by 40 per cent and offshore wind at 29 per cent.[74]

The EBRD was continuing to play a centre stage role in this trend to greater renewables deployment, now supported by falling prices, helping authorities overcome the commercial and regulatory challenges that sometimes still held up progress in an industry that could no longer be ignored.

---

72 Interview, 2021.

73 IEA Press release, October 2020. 'World Energy Outlook 2020 shows how the response to the Covid crisis can reshape the future of energy', https://www.iea.org/news/world-energy-outlook-2020-shows-how-the-response-to-the-covid-crisis-can-reshape-the-future-of-energy.

74 IRENA, 'Renewable Power Generation Costs in 2019, International Renewable Energy Agency', Abu Dhabi, 2020. https://www.irena.org/publications/2020/Jun/Renewable-Power-Costs-in-2019.

The introduction of renewables had not been easy when the EBRD pushed in this direction more than a decade earlier. But perseverance had paid off with some significant wins in some unlikely places which contributed to several countries being able to leapfrog technological alternatives.

Salkhit, Mongolia

In 2009, the EBRD made a small development equity investment in what would become the very first wind farm in Mongolia, a country otherwise totally dependent on coal for the generation of its power. The Mongolian capital Ulaanbaatar has often ranked as one of the most polluted cities in the world.

The plan was to take a small equity stake in the project to build confidence in the sector and give credibility to the project. Boyd-Carpenter says he faced a lot of early scepticism. "I was basically told this was not commercially viable," he said. But the project did proceed, cautiously at first as many hurdles had to be overcome.

In 2012, the Bank provided the construction financing and by 2013 wind turbines built on the aptly named Salkhit Mountain, 70 kilometres from Ulaanbaatar, were generating electricity and linked to the national grid. The 50 MW plant at Salkhit—meaning "Windy Mountain" in Mongolian—would generate about five per cent of the country's electricity needs and was hailed as a major step forward in the country's new green energy strategy. This was not only the country's first commercial wind project. It was the first private power generator in a sector dominated by state-owned companies.

One year later, the EBRD's investment won an award in the prestigious US Treasury Development Impact Honors list that acknowledges exceptional development projects undertaken by MDBs.

Further windfarm investments in Mongolia followed, with financing for the 50 MW Tsetsii wind farm in the south of the country in 2016 and the 55 MW Sainshand wind farm to the south-east of Ulaanbaatar in 2017.

Zhambyl, Kazakhstan

The Bank had also already pioneered renewable projects in Kazakhstan, where one particular investment had been behind a trio of firsts in the

country's solar power sector. The EBRD teamed up with the Clean Technology Fund to provide financing for a 50 MW solar plant in the Zhambyl region of south Kazakhstan, an area with a significant energy deficit.

The 2015 project, Burnoye Solar, was the first commercial-scale solar park in Kazakhstan, the country's first privately-owned renewable energy generator and saw the first use of an innovative finance structure that would open the door to more private investment in renewables in the future.

It was pioneering for the Kazakh market in its use of a non-recourse finance structure that entitled the lender to repayment only from future cashflows and not from any of the sponsor's other assets.

Potęgowo, Poland

One major milestone in the EBRD's promotion of renewable energy sources in its countries of operations was its support for Poland's return to investment in wind power in 2019. The Polish electricity market was dominated by coal and lignite-fired power plants, which contributed some four-fifths of Poland's energy mix and it faced one of the most significant energy transition challenges of any of the EBRD's countries of operations.

For several years with the Bank's help—from 2007 up until 2015—Poland had been successful in attracting investment in the renewables sector. But a number of government decisions after that slammed the brakes on the market for alternative sources of energy. The conservative Law and Justice (PiS) party had taken office after a 2015 election where they promised support for Poland's dominant coal industry. It imposed restrictions on the construction of wind farms which, alongside a penal real estate tax interpretation, meant harnessing wind power was no longer a commercial proposition.

The EBRD, alongside others, highlighted the importance of restoring investor confidence if Poland was to ensure a green transition. Gradually, the mood of the sector turned, helped by the reversal of the tax interpretation in mid-2018. That, together with the introduction of a new market-based support mechanism, again taking on EBRD advice, set the stage for a return of the wind market in an investment where the EBRD also played a significant role in the financing.

The Bank lent the equivalent of €48 million for the development of the 220 MW Potęgowo wind farm in north-eastern Poland. It marked the

EBRD's resumption of renewable energy projects in Poland, now based on support through competitive auctions, and the country's first major wind project in three years. Boyd-Carpenter said at the time the project was a turning point for the Polish energy sector:

> Three major developments have made this possible. Renewables now are at the heart of the European energy sector. In this context, Polish energy policy foresees a progressive shift away from coal to renewables. And, finally, we are in an era where renewable energy is not just a means to avoid carbon emissions; it is a source of power which does not damage air quality, does not require energy imports and which is highly affordable.

The EBRD followed up the Potęgowo investment with funding in 2020 for wind and solar parks in Poland, supporting an additional portfolio of almost 200 MW of renewable energy in what Boyd-Carpenter called a significant contribution to Poland's energy transition.

Ma'an and Risha, Jordan

As progress was made in Poland, so the renewables market gained ground in the southern and eastern Mediterranean.

One of the very early investments in the region was financing for a thermal power plant in Jordan that responded to the pressing energy needs of a country that depended on imports for more than 97 per cent of the energy it consumed.

That project, the Al Manakher power station outside the capital Amman, also anticipated a longer-term shift in Jordan's energy mix by providing the power system with the flexibility that would become increasingly important as intermittent wind and solar came to dominate generation.

Moreover, the EBRD very quickly started to work with the Jordanian authorities on the development of renewable energy sources that would tap into abundant supplies of sunshine, increase energy security and make a positive contribution to the global climate challenge.

Jordan was the setting for the Bank's first move into the renewables sector in the southern and eastern Mediterranean with an investment in a solar plant in 2014. The Bank's US$ 25 million loan provided finance for the

construction and development of a 20 MW solar PV plant outside the city of Ma'an in southern Jordan.[75]

This was the same year that Jordan had launched its own ambitious renewable energy programme. It initially set a renewable energy target of 10 per cent of generated energy, but quickly raised that goal to 20 per cent which it achieved by 2020, before setting a new target of reaching a 30 per cent share by 2030.

In late 2017, the EBRD provided funding for a new 50 MW solar plant some 300 kilometres northeast of Amman, right next to an ageing gas plant in the Risha gas fields. This new solar facility would steadily replace generation from the gas plant. It was the EBRD's eighth solar project in Jordan, adding to power capacity financed by the EBRD of over 1 GW. Boyd-Carpenter said this project demonstrated the importance of creating an "environment where the regulatory framework, the tariff design and access to finance allow for the successful use of renewable sources of energy". It was a "powerful symbol of Jordan's energy transition."[76]

Benban, Egypt

In 2019, the Benban solar plant in Egypt, the largest in Africa, started generating electricity—the culmination of years of work by the EBRD that had begun in 2014 to help the Egyptian authorities realise their ambitious renewable energy goals. The EBRD had been an important financier for the project but, more significantly, had worked with the authorities to create a backdrop that allowed the whole project to go ahead.

In the early days of the project just a small group from the EBRD, the IFC and a team of local experts worked on the project. Boyd-Carpenter recalls that there were crucial commercial and legal issues that needed to be resolved before it could move ahead. Building a solar power station was expensive, but running it was quite cheap. There needed to be a suitable commercial understanding among all parties on a Power Purchase Agreement (PPA).

Boyd-Carpenter, himself a lawyer by training, said the EBRD led the negotiations of this PPA, working with the core team of the Egyptian authorities from the Ministry of Electricity and Renewable Energy, the Egyptian

75 EBRD Press release, 27 September 2014. 'EBRD finances first solar power plant in Jordan'.

76 EBRD Press release, 11 December 2017. 'EBRD providing US$ 22 million loan to new solar power plant in Jordan'.

Electricity Transmission Company, the New and Renewable Energy Agency and their adviser Dr Mona Zulfikar, one of Egypt's leading commercial lawyers. It was just one of the many steps that were needed to create the commercial and regulatory backdrop that set the stage for Benban.

As far as the EBRD's financing was concerned, this came within a US$ 500 million framework to finance renewable energy that the Board of Directors approved on 7 June 2017 to support private renewable energy projects under the Egyptian government's feed-in-tariff programme. Finance started flowing in 2017 and by 2019 the project in the Aswan region of Egypt, 650 kilometres south of Cairo, involving 16 solar plants totalling 750 MW capacity, out of a total on the site of more than 1,400 MW, was on stream and connected to the Egyptian grid.

17. No More Coal or Upstream Oil

In 2018, the EBRD's first post-Paris Agreement energy strategy put decarbonisation firmly at the heart of its activities. The new plan emphasised a further increase in investment in renewables, promoting the switch to cleaner and more resilient energy sources in regions that continued to include some of the least energy-efficient and most polluting economies and cities in the world.

The EBRD was now completely ruling out investment in coal, which had, in theory at least, been possible under the previous 2013 strategy. In 2013, there had been pressure on the EBRD to rule out investment in coal. But some of its countries of operations were almost totally dependent on the fuel and so it announced that it would not invest in coal-fired generation except "in rare and exceptional circumstances". Any coal project would have to pass strict screening criteria and would not be considered unless it was the least carbon intensive of the realistically available options.

That was a message that kept the door open for investments for countries like Kosovo or Mongolia. In the end, this exception was not tested and there was no further investment in coal.

The 2018 energy strategy also became more stringent on investment in oil.[77] The EBRD said it would stop funding for all upstream oil exploration and, as with coal five years earlier, it would not "finance upstream oil

77 EBRD Press release, 12 December 2018. 'EBRD puts decarbonisation at centre of new energy sector strategy'.

development projects except in rare and exceptional circumstances, where such investments reduce greenhouse gas emissions".

The new strategy's focus on decarbonisation did not appease critics who were demanding that the EBRD abandon entirely any investment in fossil fuels, pointing specifically to the Bank's continued investments in natural gas. The EU-backed NGO, Bankwatch, the civil society organisation that most closely observes the activities of the EBRD, expressed its disappointment:

> Our hopes were high that the EBRD would significantly strengthen its commitments on fossil fuel lending in the final version. But reading the adopted version felt like a cold shower: indeed, the EBRD is completely ending any direct support to coal mining and coal fired electricity generation but it remains adamant in supporting gas as a transition fuel.[78]

Alex Doukas, the Stop Funding Fossils programme director at Oil Change International, an advocacy group focused on the costs of fossil fuels, wrote to the *Financial Times*, saying while the EBRD's "brand new energy strategy rules out most coal investments, it still promotes financing for fossil fuel expansion and, in particular, for polluting fossil gas".[79]

The EBRD's Managing Director for Sustainable Infrastructure, Nandita Parshad, took the criticism head on in an opinion piece for the *Financial Times*. She first addressed the coal issue, saying the damage that coal was doing to the environment could no longer be ignored: "The EBRD is responding and has now adopted a new strategy for the energy sector, which says no to coal. It is a definite position: 'no coal, no caveats'."

Gas however was a different matter. While coal was "no longer king" there was still a need for realism. Growing economies generated demand for more energy. Parshad continued: "Here, we are convinced, gas retains a critical role as a transitional fuel which is affordable, much cleaner than coal and an alternative that is critical for the coal to gas transition, especially in the EBRD regions of central and eastern Europe, the Western Balkans and Central Asia."

---

78 Ioana Ciuta, 'If the EBRD does not lead the energy transition, we will have to do it ourselves', *Bankwatch blog*, 18 December 2018, https://bankwatch.org/blog/if-the-ebrd-does-not-lead-the-energy-transition-we-will-have-to-do-it-ourselves.

79 Alex Doukas, 'EBRD should embrace its role as a transition bank', *Financial Times*, 21 December 2018, https://www.ft.com/content/1782cb5a-0465-11e9-99df-6183d3002ee1.

But the emphasis was clearly on renewables. Saying no to coal—the EBRD had not in fact financed coal for seven years at this point—was only one part of the answer. Parshad concluded:

> The citizens of those countries that rely on coal have the same right to secure affordable energy as those of other countries. This means a decisive shift towards investing in renewables, supporting the integration of energy networks, promoting the switch to cleaner and more resilient energy sources and facilitating electrification.[80]

The strategy did impose limitations on investment in gas, including a stipulation that gas should not displace less carbon-intensive sources. But there were clear benefits relevant to the EBRD region. Use of gas supported the development of renewables, which by their nature are not always available. A switch to gas from coal was a move to a cleaner fuel that reduced GHG emissions and could improve air quality. Gas development also helped countries in the transition region to deliver energy security. "Gas has multiple potential roles in the transition to energy decarbonisation, depending on country specific conditions," the strategy said.

18. Towards a Majority 'Green' Bank

The publication of the EBRD's new energy strategy came amid a new global urgency—and global awareness—surrounding the climate challenge. In October 2018, the UN IPCC issued a report widely interpreted as warning that the world had only 12 years to stave off a climate change catastrophe.[81]

Guterres called the report an "ear-splitting wake-up call to the world ... It confirms that climate change is running faster than we are—and we are running out of time."[82]

---

80 'EBRD steps up support for renewables over coal in Europe', *Financial Times*, 20 December 2018.

81 'Summary for Policymakers of IPCC Special Report on Global Warming of 1.5°C approved by governments', 8 October 2018, https://www.ipcc.ch/2018/10/08/summary-for-policymakers-of-ipcc-special-report-on-global-warming-of-1-5c-approved-by-governments/.

82 'Global warming report, an "ear-splitting wake-up call" warns UN chief', *UN News,* 8 October 2018, https://news.un.org/en/story/2018/10/1022492.

Even before the IPCC alarm call, a 15-year-old Swedish schoolgirl had been making global headlines with her demands for more action on the climate front and appeals to fellow pupils for a "Skolstrejk för klimatet" ("School strike for the climate").

Greta Thunberg's actions triggered a rising wave of support for action. Protests followed in cities across the world and intensified in 2019 bringing together millions of protestors across as many as 150 countries. Emissions were still rising and so were temperatures—hitting record highs. That June was the hottest since records began in 1880, with nine out of the ten warmest Junes occurring since 2010.

GET 2021–2025

It was against this backdrop that the EBRD began to prepare its strategy for the next five years, including an assessment of its own participation in the global response to climate change and how it would deliver on the green transition quality needed for a sustainable market economy.

Management went to the Board in June 2020 with proposals to increase the EBRD's climate action, saying the "EBRD proposes to scale up its contributions to addressing the urgent climate and environmental crisis."

The plan now was to turn the EBRD into a majority green bank by 2025, going beyond the previous 40 per cent target for green financing set for 2020:

> Reflecting a determined ambition to address these fundamental challenges, the EBRD is setting a new target to reach a green finance ratio of more than 50 per cent by 2025 with an intelligent approach to the green economy combining the commitment to the majority of its financing being green with the provision of policy expertise.

Just as the GET approach set a higher goal for green financing, so this next step would again deepen the way the EBRD approached the climate challenge.

Tanaka and his team explained their view that the EBRD now needed to shift from mainstreaming its climate activities to a new "systemic approach".

The shift to a systemic approach and greater impact included three elements: implementation of an operational framework for alignment with the Paris Agreement goals; enhanced country policy work supporting long-term low carbon strategies and greening of financial systems; and structuring

work across a set of specific thematic intervention areas to increase scale of impact, foster innovation and enhance visibility.

Ten thematic areas were defined as priority opportunities in the EBRD regions. Green financial systems, energy systems, cities and environmental infrastructure, green buildings, natural capital, sustainable food systems, industrial decarbonisation and sustainable connectivity were joined by two cross-cutting themes: energy efficiency and climate resilience.

There followed intense days of debate. The initial plan was for the Board to approve the new Green Economy Transition Approach, named GET2.1, on 24 June 2020. Specific demands from the Board, however, meant that Board formally considered the proposed approach only on 8 July and gave the plan a preliminary approval.

Directors believed the updated GET approach should become effective as part of and upon the approval of the EBRD's overall strategy for the next five years, the Strategic and Capital Framework 2021–2025. That strategy would only be approved by Governors at the Annual Meeting, which had been postponed from May until October 2020 because of the Covid-19 pandemic.

One question that was the subject of discussion was whether the scaling up of green financing would occur at the expense of other dimensions of transition impact. Directors also requested that GET2.1 include a GHG emissions reduction target which was set at 25 to 40 million tonnes per year in the period to 2025. The debate was complex as some of the highest potential GHG savings involved remedial investments in high-carbon emitting fossil-fuel based energy supplies.

Another area for attention was ensuring the integrity of the green attribution process. Here it helped that the Bank had spent several years developing green definitions and methodologies. The joint-MDB methodology for climate finance and the EBRD GET Handbook provided a good base in this regard.[83] An additional positive element was the attention it paid to ensuring effective conditionalities were attached to the green finance so that

83 Accounting for GET projects was structured around two components. On the one hand, proposals in line with the environmental and social policy and GET principles were assessed for their net environmental benefits against BAT baseline scenarios, which had to be positive to be counted as GET. On the other hand, the finance related to climate or environment components of an eligible project were identified and measured. The resulting green finance (climate mitigation, adaptation and other environmental activities) could then be compared against total EBRD finance to arrive at the GET ratio.

green results would be achieved, and that appropriate governance mechanisms were put in place.

The GET2.1 approach also involved other environmental activities including, for example, the sustainable use and protection of water and marine resources, protection and restoration of biodiversity and ecosystems, resource efficiency and pollution prevention and control. These went beyond the climate focus, while in line with the SDGs and the emerging EU Taxonomy for Sustainable Finance.

However, the major topic of discussion in the final stages of GET2.1 revolved around the timing of consideration of a full alignment of EBRD projects with the goals of the Paris Agreement. While the Bank stated that it would continue to align its investments with the principles of international climate agreements, and especially the Paris Agreement, and while it committed to implement the alignment methodology jointly developed by the MDBs, the timing question on full alignment remained open. Following rounds of discussions with Directors, the final wording approved as part of GET2.1 stated that:

> Acknowledging the intent of most shareholders, the Bank will work towards full alignment with the Paris Agreement on which a decision will be taken no later than 2022, taking into account the lessons learned from the initial phase.

Some shareholders questioned whether this was soon enough and pressure quickly built to bring this date forward—partly reflecting ambitions to accelerate climate action and commitments ahead of COP26 scheduled for Glasgow, UK in 2021, after a Covid-19 related delay in 2020.

The Bank announced the launch of what was formally called the Green Economy Transition Approach 2021–2025 in the context of approval of the 2021–2025 Strategy, on the first day of the 7–8 October Annual Meeting.[84]

Looking back on 15 years of the EBRD's contribution to climate action since the launch of the SEI in 2006, Tanaka paid tribute to the strong and consistent support received from the Board and top management of the Bank:

84 EBRD Press release, 7 October 2020. 'EBRD to aim for a majority of green investments by 2025'.

> All the Presidents—Lemierre, Mirow and Chakrabarti—stood fully behind these initiatives as they grew in stature across the EBRD. The First Vice Presidents, from Varel Freeman to Phil Bennett and most recently Jürgen Rigterink, galvanised support from all banking teams. And, our shareholders provided their very strong backing. This allowed the EBRD to become a leader in climate action showing the strong contribution which can be made by MDBs and DFIs in the battle against climate change.

Covid-19 intervenes

By the time the new proposals were adopted, in October 2020, the world was dealing with an additional and different crisis from the climate challenge the EBRD proposals sought to address.

The Covid-19 pandemic was having a devastating impact on economies across the globe, including in the EBRD's regions. On 13 March 2020, the EBRD became the first MDB to approve a coronavirus response package. On 23 April, the scale of response was increased and plans were announced to dedicate the entirety of Bank activities to fighting the economic impact of Covid-19 across its regions. The EBRD said it would invest a total of €21 billion across its regions by the end of 2021.

The GET proposals were able to reflect the additional demands of the coronavirus challenge. When the new Green Economy Transition Approach became effective on 7 October, and as he prepared to leave the EBRD after almost 30 very active years in senior roles, Tanaka made clear the new GET approach was taking the short-term challenges of the health crisis into account as well as longer-term climate demands:

> Covid-19 is a sharp warning shot about the urgency of addressing the rising climate and environmental crisis. Accordingly, the new EBRD Green Economy Transition approach identifies specific policies and investments in the short term which will support a green, inclusive and resilient recovery. And it also defines a set of actions to support its countries of operations to progress towards a low-carbon and resilient future.

His colleague Mattia Romani, who had worked with him on the GET plans, saw them in the context of a "once-in-a-lifetime opportunity to rebuild much of the global economy post-Covid-19", saying:

> Why rebuild it on the same premise as before—with high emission intensity and environmental costs—when we know that this is the past, not the future? We must use this opportunity to rebuild economies greener, fully taking into account the risks of climate change.[85]

Unsurprisingly, the outbreak of the Covid pandemic affected the GET delivery goals for 2020. The EBRD was providing emergency liquidity and working capital to partners suffering under the effect of lockdowns and the worst economic downturn in living memory.

One key element in the Covid response was the EBRD's Vital Infrastructure Support Programme (VISP) that had the double benefit of ensuring the continuity of critical public services, while also protecting the progress that countries of operations had made towards the provision of green, sustainable infrastructure.

Under the VISP, the Bank provided working capital lines to municipalities and utilities, stabilisation facilities that provided liquidity to service providers that were facing revenue losses and investment financing for public sector clients so they could continue with capital expenditure plans.

Parshad said this support was needed to maintain the momentum of a low-carbon transition and promote good governance across the sector. Launching the VISP she said:

> This is a response to the needs of our countries, cities and their citizens to keep the lights on, clean water flowing, waste collected and treated, and public transport running safely. Preserving the stable provision of essential services is vital to support those societies right now in the midst of this unprecedented crisis, but also to ensure that when the recovery comes it is a green and sustainable one, led by private enterprise.[86]

Exceptional help for clients during a year of unprecedented economic disruption meant that the Bank's finance for its operations jumped to a record €11 billion in 2020. While only 29 per cent was green, well below the 40 per cent target for the year set in 2015 and the 46 per cent achieved in

85 EBRD Press release, 7 October 2020. 'EBRD to aim for a majority of green investments by 2025'.
86 EBRD Press release, 23 April 2020. 'EBRD launches Vital Infrastructure Support Programme'.

2019, Parshad said that VISP projects had helped preserve the green agenda for the Bank and for the countries of its regions.[87]

The EBRD remained determined to reach its goal for green finance to account for more than half of its total annual investment by 2025 and steadily worked on its plans to make sure that the recovery—when it came—would be even more sustainable. As Parshad noted:

> We have set new, more ambitious green goals. This means increasing yet further the scope of our activities. It means moving from 50 MW solar plants to 50 GW plants. It means taking more risk and it means working even more intensely with the authorities in the countries where we operate, with the cities that still produce 70 per cent of the world's harmful emissions. We will work towards the electrification of urban economies and the decarbonisation of the generation of that electricity, providing the right mix of financing that will lead to a new era of clean electricity.

The EBRD's unique business model combining policy with investment would make a lasting and positive impression on the countries where it was actively supporting the transition to a low carbon future.

Shortly after taking office, Renaud-Basso described how the EBRD's new green ambitions offered a clear and structured roadmap towards a sustainable future. Reflecting on the Paris Agreement, now five years old, she wrote:

> We are now entering the decade in which key changes must be made to allow global temperature rises to be kept, if possible, to 1.5°C, making it necessary to accelerate the green transition. If we fail, the consequences will be disastrous. Meeting this challenge is not just vital, it is also doable—and financially viable.[88]

87 Interview, 2021.

88 EBRD Press release, 7 December 2020. 'Five years on from Paris 2015, the next climate challenge'.

Part III

The Role of the EBRD

Chapter 10

The EBRD after 30 Years

1. Global and Regional Challenges

The 30th anniversary of EBRD operations is taking place in the midst of a pandemic, with some observers making comparisons to the "Spanish flu" one hundred years ago. It follows other pandemics in recent years, although these were less damaging to the global economy.

This is not the only exceptional challenge facing the global community in 2021.

The past seven years have seen the top seven hottest average annual temperatures across the planet since figures were first compiled in 1880.[1] The CO_2 in the atmosphere since 2000 has increased 10 times faster than any sustained rise in CO_2 in the past 800,000 years. The change is so significant that some scientists have christened our time as a new epoch: the Anthropocene.[2]

There can be little doubt that these challenges are immense. They are present in every region and have grown in the past 30 years.

There is better news elsewhere. When it comes to standards of living the picture is less bleak. There has been a very substantial reduction in levels of poverty. Some 13 per cent of the world's population lived on less than US$ 1.90 per day in 1990: this has fallen to less than 3 per cent on the latest comparable estimates.[3]

Notwithstanding a 50 per cent increase of the world's population during this time to almost 8 billion people, incomes per capita have risen by 75

1 https://www.ncei.noaa.gov/news/projected-ranks.
2 https://www.ipcc.ch/sr15/.
3 Latest World Bank data based on 2011 purchasing power parity.

per cent,[4] and by even more in some EBRD regions such as central Europe and the Baltics.[5]

Economic growth, which is now based on a market orientation in almost all but the most fragile and conflict-ridden states, has been good overall despite the interruptions of major crises.

Most people and their families are better off in terms of basic necessities—food, access to electricity and water, secure housing. They are also significantly better connected to sources of knowledge than 30 years ago when the internet was in its infancy.

Standards of living will continue to depend on trade and economic activity being strong in the future, especially in areas where populations are rising fast such as in the MENA and SSA regions.

Yet, for all this progress, inequality of opportunity still stands in the way of a fairer distribution of the benefits of economic and social advancement. Awareness of the need to improve opportunities for all has risen but place of birth, parental education, ethnicity, age and gender continue to play a major part in determining life chances.

The world committed in 2015 to a sustainable development future by subscribing to a set of Sustainable Development Goals (SDGs) with a target of meeting them by 2030. The 17 goals seek to tackle these global and regional challenges—and more—while maintaining economic growth.

The deadline is less than nine years away. Time is short.

2. Where the EBRD fits in

The EBRD is part of the international community that aims to make a difference to development and the lives of individuals in the 38 economies in which it is active.

The EBRD's goal has always been transition. Its original task was to integrate east and west Europe as former communist countries moved away from command systems and towards market economies.

Over 30 years circumstances change.

---

4 World Bank data between 1990 and 2019, measured at purchasing power parity (constant 2017 international US$).

5 Equivalent figures for CEB were an increase of 133 per cent, while for Europe and Central Asia (excluding high income countries) they were lower at 41 per cent.

For the first half of its life, the EBRD's job was to bring market structures and disciplines to countries that had no recent experience of a market economy, and in some cases indeed no experience at all. For the past decade and a half, the task has been broader, taking in new territories bordering the Mediterranean and seeking to deepen existing but weak market structures and institutions.

The objective throughout, however, has remained the transformation of economic systems so that countries of operations can become better functioning and sustainable market economies. In so doing, the EBRD has helped them grow and develop closer to their potential.

This has meant a number of things for the way that the EBRD has operated. It has consistently made an effort to ensure that a well-functioning market system is in place. In other words, a competitive economy which encourages innovation and motivates people to succeed. It has also meant promoting the virtues of an open economy which benefits from free trade, internally and externally, and integration into the global economy.

Over time, there has been a greater understanding of the role the state can play to influence markets in a supportive but benign way. The Bank intervenes to help public authorities provide fair and effective regulations and laws and to make well-judged interventions that deal with market externalities.

But a sustainable economy, which is able to meet global challenges and the SDGs, requires more than this.

It must be resilient and well-prepared for unexpected shocks, whether from financial or other sources, as today, from the impact of disease.

It must be ready to counter the threats from climate and environmental change which have the potential to destabilise economies over the longer—but getting shorter—term, through famine, fire, flood or air pollution.

And it must pay attention to fairness and the will of the people, expressed through democratic means. Opportunities must be open to all, there must be good governance of markets and related institutions and corruption must not be tolerated.

These dimensions are captured in the transition qualities which underpin the mandate of the EBRD and its application to countries of operations. The EBRD's principles are focused on highly relevant concerns facing today's developing economies.

Principles need to be turned into practice. The EBRD has a tried and tested method for doing this. Its transition impact methodology, first

developed over 25 years ago, embeds these principles and qualities in its operational work in countries of operations.

Most projects aim to raise these countries' competitive strengths, through new products and processes that support growth, and many improve connectivity through exports and supply chains.

Around one-fifth of new projects contribute to improving inclusion outcomes, while considerable law reform activities are devoted to strengthening the governance of market institutions, making the business environment more investment-friendly, and to raising standards of corporate governance.

The Bank accelerated its operations on "green" activities around the halfway point of its life and now aims for more than one-half its business volume to be devoted to such investment-related activities by 2025.

As commercial sources of finance have expanded, the EBRD's additionality has diminished in more conventional finance products.[6] However, the Bank has been able to stretch the boundaries of investible projects and crowd in commercial finance by blending its standard finance with concessional funds from donors. Projects initiated through the use of these funds have grown rapidly in the last decade, particularly with the help of the EU and multilateral funds, mainly to support GET-related activities and infrastructure investments in less advanced transition economies.[7]

The disruption to normal life brought about by the Covid-19 pandemic prompted an unprecedented number of requests for support. As a result, the EBRD said in April 2020 that it would devote the entirety of its activities in 2020 and 2021 (expected to amount to at least €21 billion) to meeting the needs of both small and large companies in its regions facing the negative impact of Covid-19 on the demand for their products and services, and their ability to supply them.

The EBRD plays its part in helping to address some of the key global and regional challenges that its countries of operations face and are likely to confront in the foreseeable future—the consequences of the pandemic, the need for resilient economic growth, the eradication of corruption, harnessing the

---

6 Over the 30 years in which the EBRD's original countries of operations have developed, the scale of available finance in many has grown enormously. Whereas the EBRD was a significant conventional foreign investor in its region in the early days, it is less so now though it still makes similarly substantial contributions in many of the less advanced transition countries and in a crisis-afflicted country such as Greece.

7 Annual grants and other donor concessional finance have increased from well under €100 million towards the end of the 2000s to around €750 million in recent years, with about one-half supplied by the EU and one-quarter from multilateral donor funds.

potential of technology, the problem of inequality of opportunity and the causes and impacts of climate change.

3. Seven Pillars of the EBRD

In his introduction to the first volume of this history, the then EBRD President Suma Chakrabarti described the EBRD as "the indispensable bank". While he was looking to the future he was also drawing attention to the past.

In the beginning, several of the Bank's founding shareholders saw the EBRD not exactly as a dispensable bank, but as one which should not outlive its usefulness. They saw that as bringing markets and market disciplines to the former communist countries of central and eastern Europe.

This transition happened in most of these countries, with the EBRD in support. But the EBRD did not disappear.

Putting recent circumstances affecting Russia to one side, the EBRD remains active within the same geography as when it made its first investments in 1991.[8] Even the Czech Republic, the only 'graduate' of the EBRD, is returning as a country of active operations because it sees the EBRD as able to make a valuable contribution to its Covid-hit economy and to its recovery.

It is not just in the original countries of operations that the EBRD has proved its usefulness. Its expansion to Turkey and the southern and eastern Mediterranean has been widely applauded by stakeholders in these regions. So too in Greece and Cyprus, members of the eurozone.

This is not simply because the Bank offers another source of finance. It is based more on a recognition of its expertise and know-how, derived from dealing with the challenges and disruptions to markets in its original region. These countries went through similar upheavals and found the EBRD's advice especially valuable and both different and additional to support from other institutions.

While there has been waxing and waning of debate over countries' graduation from EBRD activities once they reach a certain level of advancement, there has been no similar wavering over the direction that the EBRD has taken in expanding geographically or in deepening its response to 21st century global challenges in its regions.

8 The German Democratic Republic (GDR), an original member, was absorbed into West Germany before the Bank started operations.

In short, the EBRD has turned out to be a rather useful bank.

There are several reasons why shareholders and recipients alike have found good value in the EBRD. They may be summarised in seven pillars: the EBRD is profitable, agile, private-sector led, has a strong local presence, possesses deep sector expertise, combines policy capacity with investments and applies a focused, systemic approach towards change.

Profitable

As a public institution, the EBRD offers a very efficient way of using taxpayers' money to further international development goals.

At its base is public capital. But this is only a cost to the taxpayer if it is lost or if the economic and social returns are lower than for any alternative use for the funds. There is no annual drain on finance ministries in the same way as there is from expenditure by development departments.

Provided the capital is managed carefully, the investment capacity it provides is a highly effective way to support countries to develop and grow, offering "win-win" outcomes for both the recipient countries and the providers of the capital. Reinvestment of returns builds up capital and helps expand the business and leverages additional finance. A virtuous circle is thus established and maintained.

This has been the case with the EBRD. The capital supplied by shareholders remains intact, with only €6 billion paid-in (the rest is callable), financial returns have been consistently sound and the Bank's self-generated reserves amount to nearly twice as much as paid-in funds at the end of 2020. With this capital, the Bank has delivered more than €150 billion of investment finance in over 6,000 projects in its countries of operations.

A particular advantage of a multilateral institution like the EBRD, holding capital guaranteed by a range of top-rated sovereign issuers, is that it confers a status which allows the entity to borrow in the markets at fine rates. This advantage gives the Bank the financial security to accept risks which the market does not or cannot finance.

The EBRD has held a triple-A status as judged by the leading rating agencies Moody's Investors Service and S&P Global Ratings since 1991[9] and the Bank's debt, which is treated as eligible 'High Quality Liquid Assets' in

9 Fitch Ratings has made a similar assessment since December 2002 when it first rated the EBRD's debt.

most jurisdictions, is heavily sought after by international investors looking for safe havens for their funds.[10]

Every President has cherished the EBRD's triple-A status and sought to maintain it. They have been helped by a conservative gearing policy and the vigilance of the Treasury Department, as well as by sound banking in EBRD operations. This has been especially important in recent times with several sovereigns, such as the USA, UK and France, losing their triple-A status.

The EBRD has thus offered financial advantages to its shareholders and its clients.

Agile response

The EBRD has always been an agile institution.

As a "front line" development institution, with close connections to G7 policymakers and country authorities, a staff committed to making a difference and having money at stake, the EBRD has been consistently quick on its feet.

But the key to its agility comes by virtue of it being a small, pioneering organisation, which has helped avoid unnecessary bureaucracy, allowed the fast redeployment of resources when needed and ensured unfiltered views of experts are quickly heard, and acted on, by top management.

The EBRD has stayed in tune with its leading shareholders' development goals where they have been relevant to its regions, and been ready to offer rapid support.

As a new and small IFI, the EBRD wanted to make its mark on the global stage. From the start, EBRD Presidents maintained strong links with the G7 (and later the G20) Finance Ministers' and Deputies' network that drives the official side of the international financial agenda. Its close business ties with major international banks in the private sector provided an additional perspective compared with most other MDBs.

On many occasions when the G7, G20 or the EU called on the IFIs to assist with a pressing development finance issue, the EBRD was able to contribute to a solution. It played a unique role in nuclear safety in its earliest days for example, culminating in 2017 with the final sliding in place of

10 'High Quality Liquid Assets' is a designation by a bank regulator in the relevant country of the best assets for which the banks have minimum holding requirements.

the New Safe Confinement over the Chernobyl accident site. The EBRD's first major green strategic initiative, the SEI, was launched within a year of the 2005 Gleneagles Summit which called for an MDB response on global warming. The Bank's reaction to the global and EU financial crises led to the widely praised Vienna Initiative coordination platform. And its strong partnership with the IFC on private sector development issues, for instance in response to G20 requests on additionality and blended finance, has proven highly valuable.

The EBRD has been quick to respond and able to adjust to new or rapidly changing situations, devising solutions that fit the problems as they appear. As an institution with staff from the private sector, many from its regions, the EBRD has been primed for this.

In the volatile conditions of many countries of operations, business clients often faced pressures from changing market conditions and evolving government policies. EBRD bankers had to be adept at fashioning deals to meet the particular circumstances and in this they excelled at crafting solutions in difficult conditions. Their "can do" culture spread through the organisation, facilitated by weekly meetings of an open and widely-attended cross-departmental Operations Committee, chaired by the First Vice President.

Project or client crises were frequent so procedures for dealing with them were well-tested. This made for good preparation when broader problems arose. The Bank had the mechanisms and skills in place to deal with larger crises promptly.

An especially important contribution to the Bank's agility came from staff in the field—from sector bankers talking to their clients and those in resident offices who were in touch with local business organisations and government ministers and officials. They supplied an intelligence gathering service whereby the instant that trouble was brewing in a country or sector, senior EBRD management would become aware and able to take action.

Many employees came from countries of operations and knew what might work in that context and felt a strong commitment to making a difference. They and other operational staff learned through experience how to deal with local businesses and authorities, which helped the Bank respond rapidly and effectively to new situations.

The EBRD fought major external crises all along the way. From dealing with the impact of the collapse of the Soviet system to war in the Balkans in

the 1990s and the Russian debt crisis in 1998, the Bank quickly learned how to operate in volatile and uncertain circumstances.

After a period of relative calm at the start of the millennium, a succession of crises requiring the EBRD to react swiftly punctuated the end of the first decade and into the next: conflict in Georgia, the global financial crisis and its consequences for the region, followed by the European sovereign debt crisis, the Arab Spring, economic collapse in Greece and Cyprus, revolutions in Ukraine, the implications of Russia's annexation of Crimea and conflict in eastern Ukraine and, most recently, the devastating effects of the spread of Covid-19.

The EBRD understood it was paramount to help its corporate clients and countries of operations cope with the difficulties they faced. Its clear mission—the transition of the region's countries towards market-oriented economies—was threatened by each of these crises and motivated management and staff to do the best they could to avoid the negative repercussions of these events.

These experiences made the EBRD adept at moving fast to respond to changing economic and political conditions.

Private sector led

The EBRD's unique character has made a difference to its contribution to international development.

Its private sector-led model enabled it to exploit new ideas and business opportunities, introduce new systems, products and processes, raise capacity utilisation and transfer knowledge across borders to corporates, financial institutions and SMEs in its regions.

It was able to help large and small companies—both local and foreign-owned—with its wide project size range, from transactions of less than €1 million to over €500 million. Many of its operations helped state-owned enterprises commercialise their activities and progress towards privatisation. The Bank developed a specific line of work in project preparation and financing for infrastructure projects and PPPs. In its direct financing of SMEs, the EBRD combined business advisory services alongside its investments, furnishing them with strong support.

Taking care always to be additional—not crowding out but complementing other commercial finance—the EBRD has mobilised substantial private

sector co-finance: for every euro of finance the Bank has provided, more than this amount has been mobilised from private co-financiers for a project value over three times greater than the Bank's financial contribution.

The Bank has been able to offer a full range of financial instruments, from equity (direct and via equity funds) and quasi-equity to debt and a range of guarantee instruments. It has provided financial support for debt capital market transactions, including securitised and green bonds, and mobilised significant additional finance through its syndication capacity. Risk-sharing facilities, such as first loss cover arrangements, and local currency loans in a wide variety of markets add further to the list.

Alongside its financial instruments there has been technical assistance, other advisory services and the use of concessional finance in appropriate circumstances to draw in additional private finance.

In keeping with its private sector approach, the EBRD takes risks on its balance sheet while respecting the principle of sound banking. In its lending to the private sector, which amounts to nearly two-thirds of the existing portfolio,[11] pricing is risk-based in line with commercial risk-adjusted return on capital (RAROC) models. It takes account of market conditions and is subject to robust scrutiny and risk management practices.

By taking on risks in its many investments alongside private investors—in equity and debt—the Bank has had "skin in the game". This is something private entrepreneurs understand and respect.

Strong local presence

As the biggest international investor in many countries of operations, the EBRD carried particular clout with national authorities and its visibility gave encouragement to many entrepreneurs and investors otherwise unsure whether to take risks with their savings and capital.

The Bank's client-facing approach combined with a strong local presence—"boots on the ground"—to give it strong credibility. It opened local offices very soon after it began to make investments and developed them to include banking staff, who could develop new and maintain existing

11 Under Article 11, paragraph 3 of the AEB the EBRD is required to ensure no more than 40 per cent of its total committed loans, guarantees and equity investments be provided to the state sector. See Kilpatrick, *After the Berlin Wall,* Chapter 1.

relationships with clients, as well as staff who could make links with the authorities and business community more generally.

The EBRD now has a significant reach within its regions, with over 50 well-staffed resident offices, including in many secondary cities.[12] Some regional offices, such as in Kyiv and Istanbul, have up to around 100 staff.

A strong local presence helped to open up opportunities for local enterprises, creating jobs and opportunities for less well-off members of society. Local companies and entrepreneurs also greatly appreciated the fact that bankers were able to bring in non-banking expertise—legal, environmental, economic, financial, accounting or risk—to support them.

The way in which the Bank operated as a trusted and lasting partner, sticking with deserving clients through thick and thin, and offering finance in crisis situations that no other commercially-oriented bank or institution was prepared to do was another local feather in the EBRD's cap.

Deep sector expertise

An important facet of the Bank, which helped business clients and policymakers alike, has been its deep sectoral expertise.

In all the major areas where it has invested—in financial institutions, energy and infrastructure and in agribusiness, manufacturing and services—bankers were highly-skilled and able to offer sound sector advice. When specialist knowledge was needed, as for example with energy efficiency techniques, public service contracts or capital market instruments, internal experts were available to call on.

Working with clients in situ and providing in-house expert advice meant tailor-made solutions could be found for particular country circumstances, reinforcing the Bank's value added and increasing trust.

In some areas, the EBRD was a true pioneer, spreading new knowledge and developing innovative solutions. For example, conducting sub-sovereign lending from the earliest days opened up a hugely important and successful line of business in assisting municipal utilities, helping them and other public authorities to raise their game.

Three decades of investing in water and wastewater treatment plants, solid waste management, district heating and urban transport—a unique

12 At the end of 2020, more than one-third of EBRD staff were based in its Resident Offices.

attribute of the EBRD for most of this time—put the EBRD at the forefront of this activity. The value of the Bank's expert knowledge on project preparation and feasibility of different types of project structures in municipal settings can be seen in the recent high demand for the Bank's Green Cities Programme.

Combining policy capacity with investments

The EBRD has the rare capacity to be able to deploy a full suite of financial instruments for investments, conduct policy dialogue at sector and country levels and give technical assistance where it is needed, in support of the products and services it offers its clients.

For example, policy engagement with authorities on tariff-setting methodologies, regulatory requirements and environmental standards were regular features of the Bank's work with utilities as it conducted its operations. Similarly, significant policy-related efforts were made with investments in state-owned enterprises, where commercialisation and a path to privatisation featured strongly.

Early on, policy work had a specific transactional nature as the EBRD contributed to the creation of markets by prising entities out of the state sector and into private ownership to face market disciplines. But, as the transition economies grew and their markets matured, the orientation of the Bank's policy efforts became deeper and broader as it began to focus more concretely on the sustainability of these market economies.

The Bank used its policy engagement and investments in tandem as a means of promoting reforms to support private sector development. This has become an increasingly relevant part of its work in the last decade following the stagnation of sector reforms in many countries of operations as they reached a more difficult stage of transition, and as political directions became more complicated in some.

A further aspect of policy work has been to improve the enabling conditions for investments by strengthening the investment climate and business environment.

In many cases of policy work combined with transactions, the EBRD has collaborated with other international actors, especially with the EU, IFC, EIB, IMF and the World Bank. With the pressing challenges of meeting the SDGs this is increasingly important.

Collective action involving the EBRD, as for example in the Joint Action Plans to assist central and south-eastern Europe recover from financial crises or in the Western Balkans Investment Framework, has been significant. The EBRD's collaborations with multilateral institutions to secure reform have also mattered, as in Ukraine or in addressing the heavily distorted banking sector in Moldova.

The integration of policy advice and investments by the EBRD, along-side the private sector's contributions, has featured in the Bank's thematic initiatives. This has been especially true of the Bank's climate change agenda and has been joined more recently by a strong push to provide local currency finance to unhedged clients, especially SMEs in the ETCs, and in work to develop capital markets where transition progress has lagged behind, even in the more advanced transition countries.

A focused, systemic approach

The EBRD has always had a clear mission. The Agreement Establishing the Bank, and especially its Articles 1 and 2, laid down a set of principles that has withstood the test of time. Even when the first stages of transition were largely completed, a review found that the transition concept could still provide the intellectual lodestar for the Bank's mission by focusing on sustainable market economies.

The EBRD has also always sought to generate systemic impact. Achievement of the greatest outcomes derives not so much from direct effects but from indirect effects—from the power of demonstration and dissemination of ideas and technologies, from changes in behaviour and, above all, from the results of changes to economic and management systems.

The biggest and best example, to which the EBRD's activities contributed, was associated with the Bank's origin: support for the move from a command economy, with its gross inefficiencies, to a market economy.

The first stage of this market transformation resulted in a substantial gain in countries of operations' productivity, with more than three-quarters of growth in the EBRD region up to 2010 resulting from a more efficient use of resources.[13]

---

13 EBRD *Transition Report 2013*, p. 12.

Once basic markets were in place, deeper efforts were needed to improve their functioning and sustainability, including through sector structural reforms and by advancing environmental, governance and inclusivity objectives.

This systemic approach to transition impact, combined with the principles of additionality and sound banking, created the right incentives for the Bank to push market frontiers and extend opportunities for its private and public sector clients.

The EBRD continues to pursue system change in each of the six qualities needed for a sustainable market economy, assessing its operations in each area against system yardsticks—not just the direct outcomes expected but how they will be achieved and by looking at the dynamics of their impact.

These seven pillars have served the EBRD well during the three decades of its existence. But there was also the matter of its working culture—the creative tensions and partnerships that help drive organisations forward, for better or worse.

Before turning to that, however, there is the issue of the EBRD's political mandate enshrined in the Agreement Establishing the EBRD.

4. The Political Mandate

The EBRD is the only IFI which requires that its countries of operations are committed to and applying principles of multiparty democracy and pluralism. Over the years this has raised many questions on the wisdom of Bank operations when certain countries appear to have slipped behind or departed from these norms.

Thirty years ago, when the Eastern Bloc began to embrace democracy and western values, the position was much clearer than it is today. The intervening years have clouded notions of democracy and led to a questioning of democracy's links with economic advancement, though not its association with personal freedom.

It cannot be said that progress on the democratic front, despite the Bank's urging, has kept pace with the remarkable changes seen on the economic side in the EBRD's regions.

Given the EBRD's size and its primary role in supporting private sector investment and development, the more limited impact of the EBRD in this

sphere is no real surprise. Broadly interpreted however, the political aspects of the Bank's work have served to promote a set of political values and standards expected of its countries of operations. It has done so as part of a concerted effort to bring about changes for the better and, especially in the last decade, to improve standards of public and private sector governance.

The experience of the EBRD makes clear that political economy is critical to an international financial institution seeking to build sustainable economies in emerging markets. In these countries, attention needs to be paid both to the nature of institutions—political and economic—as well as to the management of resources—human and physical—and their interactions.

Unlike mature economies, political institutions in some of these countries are not well-established and can interfere with the smooth workings of the market. Tracking and supporting their governance and development therefore matters for the delivery of the economic and political aspects of the EBRD's mandate.

As well as an economic perspective, every EBRD country strategy involves a political assessment, now based on 14 criteria, and an unalloyed description of current political circumstances using trusted reference sources. These assessments have given room for explicit Board discussions on political issues, as well as bracing discussions with recipient country authorities. The EBRD, including its Presidents, and the countries concerned each come under scrutiny in this context—one for telling it like it is, the other for explaining how it conforms to democratic values.

It can be a delicate business. There is a power to raise political issues with countries. The EBRD is unusual in that its Board votes on the country strategy including the political assessment that it contains. Many difficult conversations can take place ahead of these decisions. In cases where questions have been raised about a country's commitment to the political aspects of the Bank's mandate, strategies are designed to link the composition and scale of EBRD investments to the country's progress in reform via an approach of "more for more"; that is, the more a country reforms the more investment it can expect from the EBRD. Conversely, if a country regresses it can expect to receive less investment.

Nonetheless, bringing about change in this field is not something the EBRD has been able to do on its own. The EBRD's contribution lies in being able to reference problems in a multilateral setting, engage with the authorities—most successfully when they seek reform—and confirm the

acceptance of democratic values and the country's destination of travel. To effect change the EBRD has to be part of a wider effort.

5. Core Partnerships Behind the EBRD's Culture

The EBRD benefitted from two important partnerships—one that stretched across the Atlantic, the other mainly within the confines of its Boardroom—that often saw tensions but ultimately made significant contributions to the Bank's success. Behind them was agreement on what the Bank was ultimately trying to do, and a desire to reach common ground, even if there were different views on how to go about it.

A true multilateral: 'European character' with a trans-Atlantic perspective

Back in 1991, when the EBRD was a start-up IFI designed to foster the transition of former communist countries towards market-oriented democracies, the EBRD was a symbol of the end of the Cold War and of antagonism between east and west, especially between the USA and the Soviet Union.

Its charter—and later its *modus operandi*—was forged primarily by an agreement between countries on two sides of the Atlantic, represented by the USA and the EU. It brought together, in one place, two initially quite different conceptions of a market economy.

On the one side was the view of the private sector as the essential driver of economic growth with minimal engagement by the state and other public sector entities, while on the other public sector interventions were both an important and necessary safeguard against market excesses and an enabler of private sector development through provision of the required infrastructure.

The shareholding structure of the EBRD meant that while the USA held the largest number of shares, it could not drive the EBRD, even with the support of Japan and Canada. The EU and its institutions, in holding a majority of the shares, could. But they preferred to work by consensus. Agreement had to be found and, with various compromises made, it was.[14]

There were however common views on the appropriateness of a multilateral effort, the involvement of countries of operations in decisions and the

14 See Kilpatrick, *After the Berlin Wall,* Chapters 1 and 2.

values that underpinned market economics—especially on the rule of law and its fair application.

Tensions between sometimes radical private enterprise and market-driven ideas and a more willing acceptance of the role of the state and public investment persisted throughout much of the EBRD's life and surfaced from time to time in Board meetings over particular projects and strategies.

There were reasonable arguments on both sides. But decisions had to be made, week in week out. Just as with other successful alliances, a method was found to reach agreements.

This continuous engagement helped to balance the different views and foster a common perspective for the Bank's operations. The Bank benefitted from this strong union among its major shareholders, also supported by countries of operations whose representatives on the Board of Directors participated actively in the debates.

A real public and private partnership

There was another important partnership that stood behind the EBRD's culture of solving problems and finding a way to make public and private work together in an effective way. This was played out between Board Directors, representing shareholders, and the EBRD's management.

What distinguished the EBRD from other MDBs was not its resident Board, nor their almost daily meetings with management through committees and other discussions, although these interactions significantly helped to iron out difficulties. It was the pooling of public and private perspectives in a consensus-driven setting focused on clear goals that made the key difference.

Most Directors were officials from ministries, usually finance ministries, with long-standing public service to their name. A majority rotated after a few years in their EBRD role. Very few had a private sector background or business experience or training. Their careers and knowledge were mainly policy-based and their task was to look at the Bank from a policy viewpoint, at the impact of its activities on the transition. They were however making decisions every two weeks on operations as members of an investment bank.

The Banking Department on the other hand, represented at the Board by the First Vice President (FVP), was populated by bankers from the private

sector. Project documents set out the financial case for each investment in a way that would be familiar to any private sector investment bank decision-making committee.

The FVPs were top level international or investment bank executives with a lifetime of deal-making experience behind them, all US-based (until the most recent incumbent), and understood every last nuance behind each project—how the risks would be managed and profitability secured. However, they were also responsible for the impact of projects on the transition purpose of the EBRD.

There was thus potentially a considerable gulf in perspectives, with differences in views and understanding that were often frustrating to one side or the other. Nonetheless, the process worked.

The transaction-led nature of the EBRD and regularity of interactions between its Board and management helped keep a focus on decisions. Use was made of iterative processes where consensus was difficult to reach right away. Delivery of the EBRD's mission—its transition task to foster strong market-driven economic performance within a multiparty democracy setting as dictated by its political mandate—was always in the background to the decision-making of Board Directors and management.

Directors learned to understand what drove financial success in projects and where the risks lay. On the Banking side, attention had to be paid not just to these matters, but also to the difference their operations would make to the wider transition picture, and what additional efforts might be needed at the sector and policy level to help secure business and transition success. As policy engagements and investments by the Bank became more closely entwined, the two sides increasingly found they had more in common.

The frequent meetings, familiarity of the actors with one another and an enduring spirit of 'let's make it work', supported by Presidents with public policy experience and by independent voices like that of the Chief Economist, created a culture that melded together the best of both public and private world perspectives.

This partnership helped the Board become an effective decision-making body, which neatly combined the goals of the EBRD as an investment bank and development bank: finding profitable operations that delivered transition impact.

6. The EBRD Regions: Progress but More to Do

The EBRD's impact on transition is seen more easily in individual transactions and sectoral efforts, including in policy work with the authorities, than at a macro level. Nonetheless, it is useful to review briefly how the region, including its newer parts, has fared over this period of the EBRD's history.

Income convergence

Over the past 30 years, many countries in the original EBRD region have made progress in the convergence of per capita incomes towards those of advanced economies. However, some parts of the region remain a long way behind.

The most remarkable picture is for central Europe and the Baltics (CEB). Here, per capita incomes are now almost three-quarters (72 per cent) of the G7 average on a purchasing power parity (PPP) basis, having risen from a low point of 39 per cent in 1993 (Figure 10.1).

In the rest of the pre-2008 EBRD region, Emerging Europe and Central Asia, however, per capita incomes are around one-third of those of the G7, and only 7 percentage points higher than in 1991. They have risen substantially from their lows of just over 16 per cent in the 1990s.

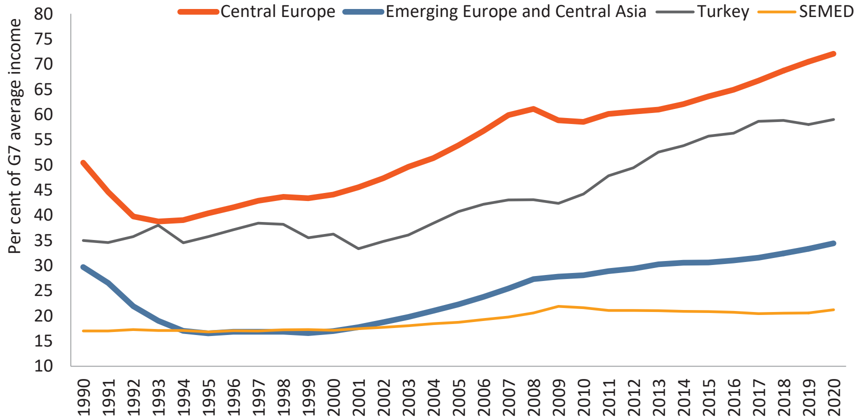
Poland provides an example of the path in CEB. It began its transition with shock therapy, recovered quickly from the initial experience of the change to its economic system and advanced steadily towards a market orientation to join the EU, less than a decade and a half later in 2004. Other central European countries did similarly well once they were able to implement market reforms.

The massive shock from the break-up of the Soviet Union took its toll on other countries, and was prolonged. The CEB had managed to start growing again within a few years after the collapse of communism, but it took until the end of the 1990s before the rest of the region managed to grow faster than the average of the G7 countries. The CEB had surpassed their 1991 position relative to G7 per capita incomes within 10 years, whereas the rest of the region was unable to do so until 2008.

Turkey's path, after its financial crisis in 2001, was similar to CEB's until it flattened off from 2017. Per capita incomes in 2019 were around 58 per cent of the G7 average. The SEMED countries on the other hand have remained stuck for a long time at a low income level, reaching only 21

per cent of the per capita incomes of the G7 in 2019, only a few percentage points higher than in 1991.

Figure 10.1 Average income per capita (PPP 2017 dollars) 1990–2020: CEB and other EBRD countries, relative to the G7 average



Source: Authors' calculations based on IMF and World Bank data.
Note: Figures are measured at 2017 US dollar purchasing power parity.[15]

Productivity

Market-driven efficiencies had the desired effect that policymakers hoped for in the first period of transition. There was a striking improvement in total factor productivity (TFP) in EBRD countries of operations in its first two decades:

> As countries emerged from the initial transition recession, the catch-up in terms of TFP levels enabled by the broad market-oriented reforms was the single most important factor that supported fast income convergence between the mid-1990s and the end of the next decade. No other region experienced such fast productivity growth as the transition region.[16]

15 In cases where GDP measured at market exchange rates and purchasing power parity differ considerably, as in Turkey's case for example, the figures may flatter the relative position to G7 countries (where this discrepancy is generally small).

16 Y. Georgiev, P. Nagy-Mohácsi, and A. Plekhanov, 'Structural Reform and Productivity Growth in Emerging Europe and Central Asia', June 2017, https://www.adb.org/publications/structural-reform-productivity-growth-emerging-europe-central-asia.

Estimates suggest, however, that total factor productivity made little significant contribution to growth in the following decade other than in Central Asia. With capital utilisation falling as a result of the global financial crisis, TFP may even have been a negative influence in some EBRD regions. Capital accumulation appears to have been the major influence on growth during this period.[17]

Labour productivity continued to grow during the EBRD's third decade, but only slowly compared with the previous 10 years, at an annual rate of just over 2 per cent.

GDP growth

Before the global financial crisis, the annual GDP growth across the original EBRD region from the start of the transition averaged under 2 per cent, but was higher in CEB (3.2 per cent) and Central Asia (2.6 per cent). For sub-regions outside CEB, however, the figures disguise the sharp falls in output seen during the 1990s, which were followed by a strong recovery until 2009 when growth turned negative once again.[18] This pattern is shown in Figure 10.2.

Like productivity, output growth was noticeably slower after the 2008–09 financial crisis compared with its average from the turn of the millennium, falling back particularly sharply in Russia and eastern Europe and the Caucasus (EEC) to barely 1 per cent a year and low figures for emerging economies. Table 10.1 shows that during this time annual growth in south-eastern Europe was a bit more than 2 per cent.[19]

After a modest fall in 2009, post-crisis output in CEB recovered strongly, limiting the fall back in growth, to record an average annual rate of 2.7 per cent between 2009 and 2019. Central Asia did even better (5.4 per cent), and growth rates improved relative to the period from 1991.

Since the start of the transition, the average annual growth of 3.0 per cent in CEB and 2.1 per cent in south-eastern Europe stand in sharp contrast to the figures of 0.6 per cent and 1.0 per cent for EEC and Russia, respectively. The latter is especially weak in view of commodity price increases during

---

17 See 'Sustaining Growth', EBRD *Transition Report* 2017–18, pp. 16–17, and Charts 1.11 and 1.12 in particular.

18 Other than in Central Asia where positive growth of 3.5 per cent was recorded in 2009.

19 The definition here excludes Greece and Cyprus.

this period, which helped to bolster average growth rates for example in Central Asia to 3.7 per cent a year.

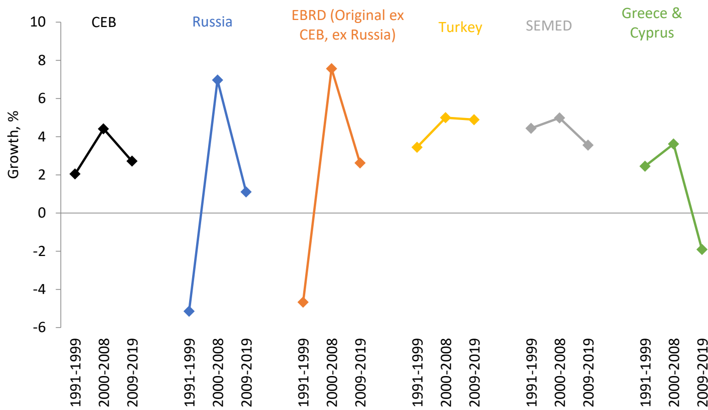
The faster growing economies of Turkey and the SEMED countries boosted overall growth in the EBRD regions as a whole in the decade to 2019, although only Turkey raised its growth performance between this period and the one from 1991–2008.

Table 10.1 Average GDP growth rates in EBRD regions, 1991–2019

GPD growth rates, annual average, %	1991-1999	2000-2008	2009-2019	1991-2019
EBRD	-1.0	6.0	2.5	2.5
EBRD (Original Region)	-3.0	6.4	2.0	1.8
Central Europe and the Baltic States	2.0	4.4	2.7	3.0
South-eastern Europe	-1.9	6.0	2.2	2.1
Eastern Europe and Caucasus	-7.4	8.4	0.7	0.6
Russia	-5.1	7.0	1.1	1.0
Central Asia	-3.5	8.7	5.4	3.7
Turkey	3.4	5.0	4.9	4.5
Greece & Cyprus	2.5	3.6	-1.9	1.2
Southern and Eastern Miditerranean	4.4	5.0	3.6	4.3

Source: Authors' calculations based on IMF and World Bank data.
Note: Some observations for countries that did not exist are missing for early years.

Figure 10.2 Average GDP growth rates in EBRD regions: the 1990s, pre- and post-global financial crisis



Source: Authors' calculations based on IMF and World Bank data.
Note: Some observations for countries that did not exist are missing for early years.

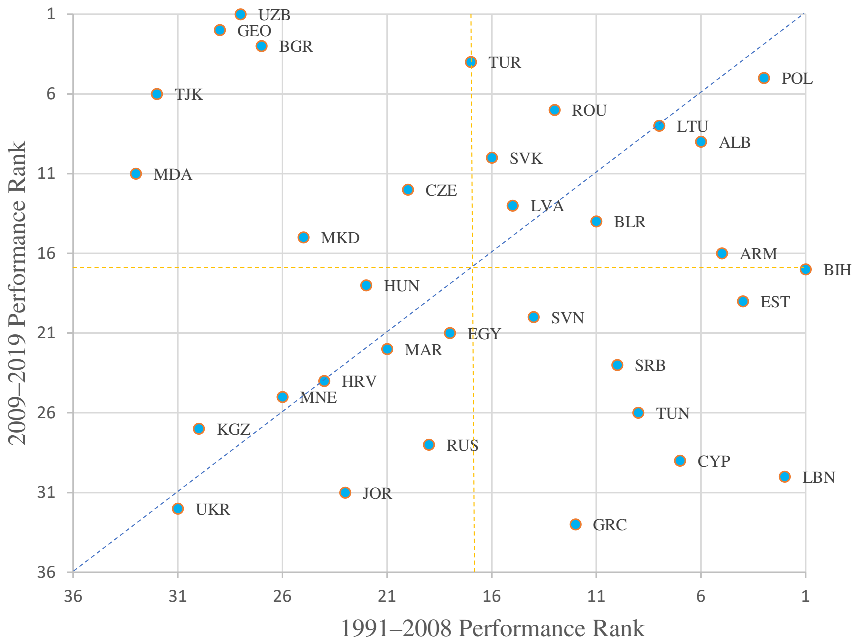
Country performance pre- and post-global financial crisis

A comparison of the performances of countries in receipt of EBRD finance, based on rankings of GDP per capita growth before and after the global financial crisis, shows how some countries have performed well throughout the period, and others that have done well post-crisis. (Figure 10.2).

Consistently good performances through 1991 to 2019, shown in the top right-hand quadrant of the Figure 10.2, occurred in Poland, Lithuania and Albania for example. At the other end of the scale lie Ukraine, Jordan, and Kyrgyz Republic.

The most improved per capita growth performances in the post-crisis period (top left-hand quadrant and distance from the 45° line) have been in Uzbekistan, Georgia, Bulgaria and Tajikistan. Most affected in the other direction were Lebanon, Cyprus and Greece.

Figure 10.2 Relative per capita GDP performance of countries of operations, 1991–2008 and 2009–2019



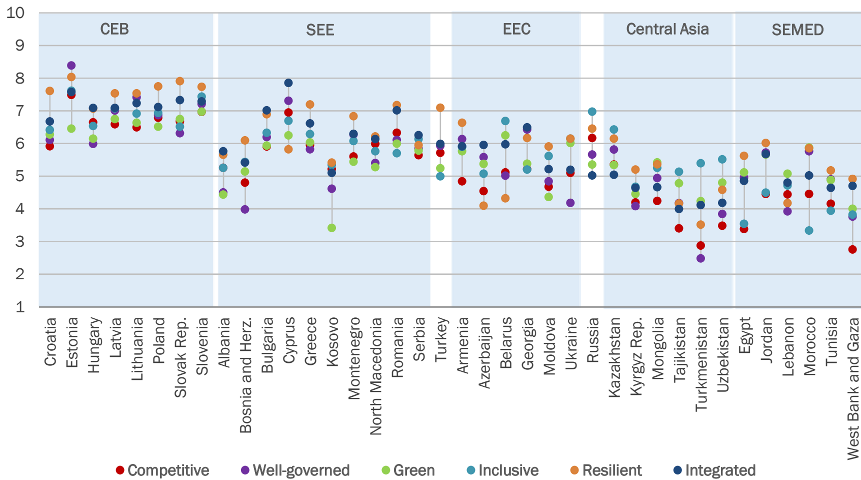
Source: Authors' calculations based on IMF and World Bank data. *Note:* Countries are ranked on average growth rate of GDP per capita in each period and the ranks are then compared.

Structural reform

The assessment of transition qualities presented in the *Transition Report* shows the distance of countries of operations from a synthetic frontier representing the position of a fully sustainable economy for each quality. Figure 10.3 shows the latest pattern.

Among EBRD regions, CEB countries show a clear lead, with Estonia at the top of five qualities and Slovenia showing a strong and consistent performance, including best performer in the 'green' category. By contrast, West Bank and Gaza, Kosovo, and Turkmenistan are a very long way behind, particularly in the well-governed and resilient qualities in Turkmenistan's case. Elsewhere, Morocco, Egypt, Tajikistan, and Uzbekistan have catching up to do in a number of transition qualities.

Figure 10.3 Indicators of structural progress by EBRD countries of operations, 2020

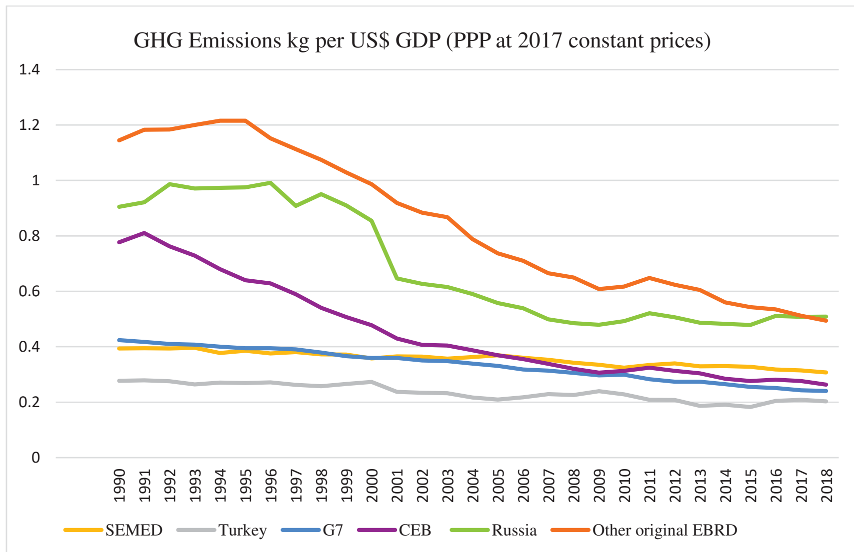


Source: EBRD *Transition Report 2020–21*

Energy intensity

The EBRD's focus on energy efficiency from the start of its operations was driven by the very high energy intensity of its countries of operations. Encouragingly, there has been good progress in the reduction of energy intensity in this region over the past 30 years.

Figure 10.4 EBRD regions and G7 GHG emissions per US Dollar of GDP at PPP, 1990–2018



Source: Authors' calculations based on Climate Watch and World Bank data.
Note: 'Other Original EBRD' countries are those in south-eastern Europe, Russia, EEC and Central Asia.

GHG emissions per US dollar of GDP (at PPP) have fallen threefold in CEB, and by more than one-half in the rest of the original EBRD region (excluding Russia) during this time. Emissions in Russia have also halved but, unlike other original EBRD countries, the trend has been flat for over a decade. In all these cases, emissions per unit of GDP are now much closer in absolute terms to the average of G7 countries, with CEB very close to the G7 level.[20] (Figure 10.4).

In the case of Turkey and SEMED, emissions per unit of GDP have been relatively low. In these two regions only Turkey has maintained a level consistently below the G7 average, though there has been little change since the mid-2000s, while SEMED has made some progress since then but is now some way above the G7 average.

Despite the significant falls in GHG emissions per unit of output in south-eastern Europe, Russia, eastern Europe and the Caucasus and Central Asia, the overall rate of decline has slackened somewhat in recent years and the level

20 The G7 figure is strongly influenced by the relatively high level of the USA's GHG emissions, which fell from 0.55kg to 0.29kg CO_2 equivalent per US$ GDP (PPP at constant 2017 prices) between 1990 and 2018.

remains twice as high as in the G7 and CEB, and even more compared with Turkey. Significant efforts will be needed to match performances elsewhere.

More to do

In sum, the picture of the EBRD regions is one of good progress in several areas but that there remains a lot more to do. The current Covid-19 pandemic makes this all the harder but even more important.

7. The EBRD Contribution

This history has described how in various ways the EBRD fostered the transition of its countries of operations towards more open and sustainable market economies.

There have been many advances, as the previous section noted and as the EBRD's annual *Transition Reports* have documented in more detail over the years. However, a full disentangling of the contributions of the EBRD from everything else that was happening in the rapidly changing circumstances of these countries is a close to impossible task.

At a micro-level, many transition indicators, country reviews, client surveys and internal project scores suggest that the EBRD made a genuine difference to businesses and economic development in every region in which it has worked. Although rates of progress differed—across regions and over time—significant changes have occurred right across the EBRD's regions over the 30 years of Bank operations.

The long view

The independent Evaluation Department (EvD) has looked in detail at many projects and strategies from the start of the Bank's operations, identifying their strengths and weaknesses, talking to clients and making suggestions for improvements. However, when it comes to reaching a considered answer on the impact of the EBRD, Joe Eichenberger, EvD's Managing Director of 10 years,[21] admits it is difficult to offer any simple conclusion.

21 Eichenberger joined the EBRD in January 2011, after spells as Vice President at the African Development

One aspect of importance, he recalls, was the EBRD's role in supporting FDI in the 1990s. "In the first decade the EBRD was substantially associated with FDI. That matters for its enduring legacy", he says. Sustained engagement at times of great challenge is also important, with Ukraine an example of that long-term commitment: "After the protests in 2014, at a moment of deep crisis and peril in that country, the EBRD was the single largest lender. For a small regional institution in the context of a relatively large and important lynchpin country, that was a substantial contribution."[22]

In Eichenberger's view, the EBRD offered steadiness and reliability. During the global financial crisis, he says that the EBRD set an example of an institution "without a mandate for countercyclical activity moving with real speed and capitalising on its client relationships to create a signal effect."

As a relatively small organisation in which key relationships are with private clients, the EBRD is positioned differently from more traditional development banks. Unlike in those institutions, Eichenberger notes, there is little 'programme capture' at the EBRD—the tendency for internal resources to be spent on keeping big programmes alive or funded. Instead, the attitude is more one of deploying funds if they can be useful but otherwise move on. "That's a very different cultural character. It's pragmatic, it's delivery-oriented."

He suggests this culture—driven and outward-looking—was strongly influenced by the EBRD's early "near death" experience and the restructuring that followed under President de Larosière and his First Vice President, Ron Freeman.[23]

> Those events, the trauma, absolutely created inside the EBRD a dynamic of "we've got to get things done". It was a terminal moment that shaped the personality of the place from the very outset, leading to this powerful cultural characteristic.

He is also impressed by how much policy-solving work goes on below the radar, by drawing on experience and "pockets of expertise across the

Bank and the Asian Development Bank and, before that, US Treasury Director of the Office of Multilateral Development Banks and acting Executive Director at the World Bank.

22 Interview, 2021.

23 See Kilpatrick, *After the Berlin Wall,* Chapters 3 and 4.

Bank" with "bankers taking an active interest in [relevant] issues". He believes this "distinctive aspect of the EBRD offer to clients" has helped "keep the Bank in demand."

Alain Pilloux, a highly experienced banker who joined the EBRD in 1992 and is now Vice President for Banking, believes the Bank's role in mitigating risks was a significant plus for investors in the early days, especially for foreign players, and mattered more than the finance. There were many examples of rogue behaviour by individuals, judges and authorities where the EBRD's interventions helped resolve difficulties for its clients and improved countries' understanding of western business practices, he says.

Even more important, in Pilloux's view, was the EBRD's contribution to the emergence of local middle class entrepreneurs, supporting a growing *mittelstand* in countries of operations.

> Nowadays, 80 to 90 per cent of Bank activity is with local businesses. We have spent our lives supporting, encouraging and financing local people with ideas and ambitions. Our model is to make investments of a modest average size but to do a large number of them. The multiplication of these transactions with local players has had a significant impact in every single country, in all EBRD geographies. Overall, it is the core value add of the EBRD over the last 30 years. Not only has it supported sustainable growth in those countries, by relying on local production and local players' ideas and innovations, but it has also contributed to the anchoring of democracy.

Pilloux sees two other aspects as valuable. "Reliability is a major attribute of the EBRD," he says.

> There is a general sentiment among clients that the EBRD can be relied upon whether the sun shines or not. This was proven in the 2008-2009 crisis and now during the pandemic. [Business] people may complain about the fact we require high standards and that due diligence can be cumbersome or a bit long. But even those who complain the most, they always return. We manage clients in a smooth way and are known for our flexibility. And our large presence in the field is a jewel, an extraordinary asset of the EBRD, especially with the pandemic.

And then there is the "unique way" in which the EBRD integrates policy and business which "concentrates on those aspects or reform that unlock investment and growth".

> We work beforehand on legislation, and with the authorities, helping to design the processes which lead to practical and concrete investments, and then we help to implement them. As in renewables for example.[24]

Views of four Chief Economists

In gathering to celebrate 30 years of the EBRD, three former Chief Economists, and the current incumbent, expressed their views on the role and impact of the EBRD.[25]

Looking back at the importance of the Bank's founding charter, Nick Stern, the EBRD's second Chief Economist, commented:

> It's remarkable how solid those principles of the EBRD have been. Article 1 on open market economies ... Article 2.1 (vii) which has environment in it quite explicitly, and sustainability too. The people who wrote [these] did a very good job. It's those first principles, and of course fundamentally sound banking, additionality and transition impact, [that give] the logical structure need[ed] to drive the whole story forward.

He pointed to three "multipliers" behind the EBRD that make a difference:

> The EBRD has the advantages of a development bank, of being on the frontier and moving as the frontier moves. That embodies the power of example, the multiplier of example. [Then] we have the multiplier of the private sector, through the management and reduction of risk, and the multiplier of collaboration with other IFIs to share risk in different ways and to create the policies, frameworks and platforms to foster investment.

For Erik Berglof, the EBRD contribution has come through its "large staff on the ground and a unique business model which developed over

---

24 Interview, 2021.
25 EBRD Press release and podcast, 16 April 2021. 'The EBRD at 30: what's next?'.

time, combining engagement with the private sector but also engaging with the state to build the private sector." Beata Javorcik sees the EBRD as the "ultimate impact investor", sending a signal whereby impact goes beyond an individual project, while Sergei Guriev, noting the private sector development bank role and its impact in creating a competitive business environment, says "countries and businesses know that if they're partnering with the EBRD they will use technology and business models that are the future."

When it comes to the more visible changes over 30 years, a great success of the transition, Javorcik says, is that "young people today [in the region] feel no different than their peers in western Europe." Stern adds that "the rise in living standards and the ability to choose have been quite spectacular."

For Guriev, it is the creation of a new services sector, in which the EBRD played a key role. Not only in its most visible form of shopping malls and entertainment centres (one such EBRD investment for example being in Surgut, Siberia), but also in knowledge-based areas such as pharmaceuticals (such as Petrovax in Russia or Hikma in Jordan), and in the use of new technological platforms (as with MICEX-RTS, Yandex or UiPath).[26]

He explains that the EBRD assisted with the move out of heavy industry towards a services-based economy—in part the consequence of introducing market forces and helping to make them work—"where you create businesses which provide middle class jobs and services that are much needed and make life in these countries so much better." Continuing, Guriev said:

> The EBRD's job was to create systemic impact, to change the whole economy. In many countries you can see that the leading companies in the services sector are EBRD clients. This is a great achievement.

On other impacts in its regions, Javorcik emphasises the EBRD's role in helping with privatisation and improvements to the governance of state-owned companies, even if "it's by no means done".

Stern says the impact of the EBRD has to be seen in the context of its overall story, especially its role in making a market economy function well. But, he notes, "the skills that the EBRD developed in particular areas were

26 The EBRD's interest in Yandex and UiPath was through its investments in private equity funds managed by Baring Vostok and Earlybird Venture Capital (Digital East Fund), respectively.

extremely important," for example with an early and sustained effort to build up its energy efficiency capacity.

Berglof says it should not be forgotten how the original EBRD countries of operations "came into the transition without anything remotely resembling what we think of today as financial systems".

> The EBRD played a very important role in building financial systems in its countries ... and using them as delivery mechanisms, for trade credit, for targeted credit lines for energy efficiency and for women entrepreneurs. That has changed opportunities for people and allowed different parts of these countries to develop. Using the financial sector to achieve development aims—that for me is the single most important achievement.

Stern concludes that "as well as helping [with] the change in living standards and institutions we should recognise also the influence of the EBRD on what a good development bank is."

> I was very much involved in setting up the AIIB and NDB[27] and we had very much the EBRD as a model. [We said] look at what it does, look at its articles of association, look at its emphasis on the private sector, look at its emphasis on additionality and being on the frontier and on transition impact. That's the model you should use.

Furthermore, Stern says:

> It's going to be really important moving forward because if we're going to make investments that take us to net zero [emissions] the development banks are absolutely centre stage, ...[they] have never been more important. The EBRD is the best model of these.

Some external perspectives

Many of the international organisations the EBRD has worked closely with during this time appreciate the role it plays in the region. The IMF Managing

27 The Asian Infrastructure Investment Bank (AIIB), based in Beijing, and the New Development Bank (NDB), based in Shanghai. Both banks were established in 2015 and opened for business in 2016.

Director Kristalina Georgieva notes how, after contributing to "building a new, post-Cold War era in central and Eastern Europe", the EBRD "evolved to support the drive towards market-oriented economies on three continents: Europe, Asia and Africa". She says today's EBRD support "remains just as critical to help economies transition to a post-Covid world."[28]

Christine Lagarde, Georgieva's predecessor at the IMF and now President of the European Central Bank, has commented on "the fantastic partnership that we've had together, EBRD and ECB, particularly during the great financial crisis under the Vienna Initiative".[29] And the current President of the European Commission, Ursula von der Leyen, says: "In 30 years you have achieved so much. You are a unique institution—a true bridge between the European Union and our neighbouring countries."[30]

Perhaps the best testament to the EBRD's impact comes from the views of people in countries of operations themselves. There are many examples of clients who value the contributions made by the Bank to the success—and survival—of their projects.

One example comes from Levan Mebonia, Chairman of Enguri Hydro Power Plant in Georgia which supplies 40 per cent of the country's electricity, who was an engineer when the EBRD first invested over 20 years ago. He says:

> The plant was in a very dire state. With the EBRD's support its dam and tunnel became safe and we now produce twice as much energy as before. The EBRD has a very good reputation in Georgia. Everyone knows that projects funded by the EBRD will be completed and be well done. I personally cannot imagine a better partner than the EBRD.

Another example comes from National Bank of Greece, one of the largest commercial banks in that country, reflecting on its long-term strategic partnership with the EBRD in Greece and elsewhere in south-eastern Europe. It said in a statement that the "EBRD's investments have been instrumental in enhancing resilience, supporting restructuring and enabling re-establishment of access to international capital markets."[31]

---

28 Interview, 2021.

29 Interview, 2021.

30 Interview, 2021.

31 Statement to the EBRD Resident Office, 2021

Seen from Belgrade, one local EBRD senior officer, Svetlana Strizovic, says a key factor for local clients has been the consistency and quality of advice. "They see [the EBRD] as a very reliable partner. As soon as the EBRD is involved, it lifts everything up onto a higher, more trusted level." When there is a crisis, she says, "The Bank deals with it in a very British way: toughen up and carry on. The Bank does not lose its wits and keeps a steady course. This has been an inspiration."[32]

The sense of long-lasting partnerships to support countries' transition progress is echoed by the Turkish Ministry of Treasury and Finance:

> Cooperation with [the] EBRD has not only brought alternative financing to the country, but also provided crucial technical assistance, international best practices, high standards and good governance principles to the private sector as well as to the public sector. In this regard we call EBRD lending as [a] quality partnership.[33]

8. A Model for the Future: Coordinated Multilateral Solutions

The EBRD has an appealing business model when it comes to raising the level of private finance for development and engaging private businesses in finding innovative solutions for global and regional problems.

The Bank could do more with its existing capital, not just to help deal with the consequences of the Covid-19 epidemic and climate change, as it is doing now, but also—should shareholders agree—to support potential transition countries further afield in MENA and parts of sub-Saharan Africa, which have close ties to Europe but have important development needs, including better functioning markets.

The EBRD, nonetheless, will always be too small on any measure to make the critical difference on its own. Its model will be most effective when coordinated efficiently with other DFIs, which would be consistent with the conclusions of the 2018 G20 Eminent Persons' Group report *Making the Global Financial System Work for All*.[34]

---

32 Interview, 2021.

33 Information supplied by the Turkish Ministry of Treasury and Finance, January 2021.

34 'Making the Global Financial System Work for All', Report of the G20 Eminent Persons Group on Global

Billions to trillions: the role of the private sector

In its submission to the Development Committee for the 2015 World Bank/IMF meetings, the EBRD, other MDBs and the IMF pointed to the wide range of domestic and international financing options beyond official development assistance (ODA) that was available for development. They stressed that all these channels would be needed to support and accelerate the scaling up of finance for development to move from 'Billions to Trillions'. The international community recognised the critical role that private sector finance could contribute to meeting the SDGs.

The Paris Agreement on Climate Change later that year, and the national commitments made by 189 countries to increase investment in a low-carbon future,[35] paved the way for the important part the private sector can play to keep the rise in global temperatures to manageable levels.

Less attention was paid, however, to models through which the public sector could play its part in this effort and efficiently engage with the private sector to reach these goals.[36]

The EBRD model of using public capital to work with and draw in private finance for development is an important one. It relies on alignment of interests in a market context to generate finance for the investments needed to effect change. Market signals are an important driver of change, as we see today with consumers increasingly taking climate change and other environmental dimensions into account in their product choices.

Transforming weak markets to become more robust and ensure their signals are transmitted clearly and effectively has been a backbone of the EBRD's work. Where signals are missing or distorted by externalities, the EBRD has had the means to step in and help the private sector take on additional risks or, where this cannot be achieved, find efficient public sector solutions.

Multilateral development banks have been the traditional means to date for tackling development issues. Yet over the last three decades global finance

---

Financial Governance, Tharman Shanmugaratnam (Chair), October 2018, https://www.globalfinancialgovernance.org/assets/pdf/G20EPG-Full%20Report.pdf

35 Renewable energy, energy efficiency, sustainable infrastructure and climate-smart agriculture were mentioned.

36 An exception is the IFC's report 'Creating Markets for Climate Business', published in 2017, which describes how US$ 23 billion of investment opportunities could be exploited with the help of the private sector.

has been dominated by the private sector. The link is only now getting the wider attention it deserves. It has been present all along in the EBRD.

The EBRD is one of only a handful of financial institutions that has successfully shown how private sector finance can be harnessed alongside public funds for public purposes. The EBRD's approach, in coordination with others deploying similar models, appears to be a valid—and scalable—way of using limited taxpayer funds to meet development and climate change goals.

Sub-Saharan Africa: geographic expansion once more?

In recent years, the Bank has looked into further areas of possible geographic expansion, in particular to a limited number of countries in sub-Saharan Africa and to Iraq. According to its latest strategy: "The context … was … geopolitical and development priorities, as well as the growing links between many countries in sub-Saharan Africa and Iraq and current EBRD countries of operations."

Large unmet needs in these countries, where progress on the SDGs is lagging, implies a role for private sector development where certain minimum conditions of stability and security exist and where there is a willingness and ability to build on existing market conditions. The EBRD sees itself as a complementary actor to other development finance institutions, as it has been in its previous expansions, with its transition mandate, private-sector led business model and full set of financial instruments able to add value.

The 2021–2025 Strategic Capital Framework (SCF) explains the importance of the additional contribution that the EBRD could make: "Private sector development will be key to supporting jobs and better livelihoods and providing the basic services and infrastructure all people need. This will decrease the risk of social unrest and help reduce levels of unplanned migration."[37]

The EBRD has shown in several previous geographic expansions—and in facing up to many crises—that it has the capacity to adapt quickly and flexibly to new situations.

The debate on a possible expansion into sub-Saharan Africa and Iraq is set to continue. Governors are expected to give direction at the 2021 Annual

37 Strategic and Capital Framework 2021-2025, September 2020, p. 44.

Meeting in London on further preparatory work to be undertaken to allow the consideration of any next steps at a subsequent Annual Meeting.

Towards a New Era

A capability for MDBs to work with the private sector and accelerate finance for development is essential for the future. The EBRD has evolved as a reliable private sector-focused institution with a proven track record over its 30 years, encompassing several geographies and coping with many crises.

The EBRD is proof that public and private sectors can work well together when they have clear goals and the right incentives. The model has demonstrated wide applicability.

Looking back over 30 years to when the EBRD started operations in 1991, we might ask what a 30-year-old then involved in creating the EBRD might have seen in the future institution.

They would have been born in 1961, the year the East German government started building the Berlin Wall, the most visible symbol of the Iron Curtain that divided east and west.

It is perhaps no surprise that when the Berlin Wall fell, and the Cold War era ended, our 30-year-old saw market-oriented democracies as a way forward for both sides of the divide with the EBRD as a way to help this process. The hope was that at last peace and prosperity could reign in Europe.

Looking back further it is worth recalling the succession of conflicts that would have coloured the thinking of similar 30-year-olds during the 20th century. One born at the end of the Victorian era would have been scarred by the experiences of World War I; their counterpart born 30 years later lived through the Great Depression and World War II; and then, for our new EBRD-er, came the possibility of World War III—and the overshadowing threat of nuclear war and the annihilation of Europe.

Today's 30-year-old, born in the same year as the EBRD, has not lived under the reality or the shadow of world war. Globalisation has driven the biggest reduction in poverty in human history. Peaceful international connectivity has perhaps never been greater.

But this Panglossian end to the story misses out an important new existential threat. That of climate change. No longer the risk of a sudden clash of powers perhaps, or imminent death, but a relentlessly growing threat to

the quality of human existence and the future of the planet itself. It cannot be left unchecked.

What war was to the 20th century, climate change is to the 21st. It calls for the same comprehensive mobilisation of political will and effort.

Clausewitz regarded war, inter alia, as the "realm of uncertainty ... the realm of chance", making intelligence and judgement crucial. In this context, he wrote:

> Two qualities are indispensable: first, an intellect that, even in the darkest hour, retains some glimmerings of the inner light which leads to truth; and second, the courage to follow this faint light wherever it may lead. The first of these qualities is described by the French term, coup d'oeil; the second is determination.[38]

The EBRD has shown these qualities.

It saw the light on climate change early on and had a vision how it could develop market-based solutions to tackle global warming and help bring about the transformation required. The EBRD was ahead of its time, as it has been in other areas.

It showed determination in its efforts to harness the private sector in support of public goals, in its region and beyond.

The EBRD has done so by fostering economic growth through better market performances and greater resilience, through trade and integration and by encouraging innovation and entrepreneurship. It continues to transform market economies, making them more sustainable by being better governed and more inclusive. Above all, it is helping to lead a transition towards net zero greenhouse emissions by invoking private sector-oriented solutions and operating at the frontier of public and private finance.

The EBRD has shown a way forward on development. The international community should not dither over architecture. There is already a well-tuned model and the world needs all the resources it can muster to complete the tasks.

This is indeed why, 30 years on, the EBRD remains an essential development bank.

---

38 Carl von Clausewitz, *On War*, Chapter 3 'On Military Genius', translated by M. Howard and P. Paret, edited by B. Heuser (Oxford University Press, New York, 2007), p. 47.

Jean Lemierre, EBRD President (2000-2008). © EBRD

Thomas Mirow, EBRD President (2008-2012). © EBRD

Suma Chakrabarti, EBRD President (2012-2020). © EBRD

Odile Renaud-Basso, EBRD President (2020 -). © EBRD

Nick Stern, former Chief Economist of the EBRD (1994-1999) visits the Bank as an alumnus in 2016. © EBRD

Josué Tanaka, a former EBRD Managing Director, led the Bank's Energy Efficiency and Climate Change activities until 2020. © EBRD

Sergei Guriev, Chief Economist of the EBRD (2016-2019). © EBRD

Barbara Rambousek, Director for Gender and Economic Inclusion at the EBRD. © EBRD

Nandita Prashad, currently Managing Director, Sustainable Infrastructure (SIG) at the EBRD. She previously led the Bank's Energy & Natural Resources Business Group. © EBRD

Hans Peter Lankes, Managing Director, Institutional Strategy (2011-2017). © EBRD

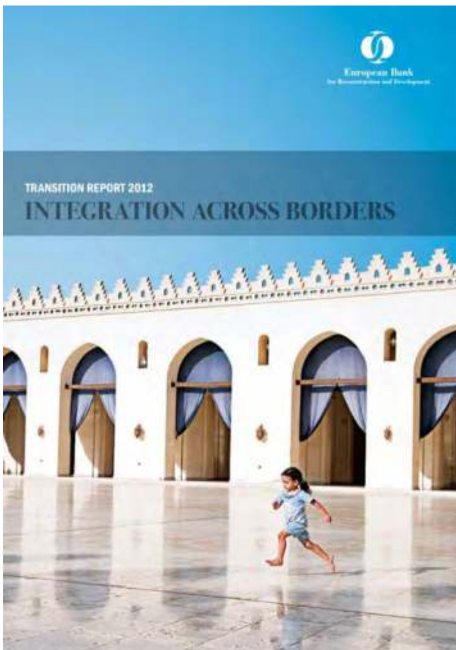
Hildegard Gacek, first Managing Director for the southern and eastern Mediterranean (SEMED) (2012-2017). © EBRD

Erik Berglof, Chief Economist and Special Adviser to the President (2006 to 2015). © EBRD

G8 leaders pose for a family photo at the end of the G8 summit in Gleneagles. Front row L to R: U.S. President George W. Bush, French President Jacques Chirac, British Prime Minister Tony Blair, Russian President Vladimir Putin, German Chancellor Gerhard Schroeder. Back row L to R: Canadian Prime Minister Paul Martin, Japanese Prime Minister Junichiro Koizumi, Italian Prime Minister Silvio Berlusconi, President of the European Commission José Manuel Barroso. © Alamy Stock Photo

As part of the UK's G8 Presidency, Britain hosted the G8 Deauville Partnership Investment Conference in London on Monday, 16 September, 2013. Left to right, Ahmad Mohamed Ali Al Madani, President of the Islamic Development Bank (IsDB); Alistair Burt, Parliamentary Under Secretary of State at the UK Foreign and Commonwealth Office; and Suma Chakrabarti, EBRD President. ©www.gov.org.

Amman, Jordan. The EBRD began investing in the southern and eastern Mediterranean (SEMED) region in 2012, in the wake of political upheaval in the Arab world. The Bank's first Annual Meeting and Business Forum in SEMED was held in Cyprus in 2017. © EBRD



The *Transition Report 2012: Integration across Borders*, analysed the progress and future challenges in countries of the southern and eastern Mediterranean (SEMED) region, where the EBRD had recently extended its operations. © EBRD

The *Transition Report 2013: Stuck in Transition?* showed how emerging countries were in danger of forever trailing the living standards of more advanced market economies, but argued that they could still break through obstacles to greater prosperity. © EBRD

Istanbul, Turkey. Turkey became an EBRD country of operations in October 2008. Within seven years, it became the Bank's largest country of operations. © EBRD

Turkey's third-largest city, Izmir, has expanded its light-rail system with a comprehensive financing package put together by the EBRD and its partners. © EBRD

The EBRD is a leading agribusiness private sector investor in countries such as Ukraine, where the Bank focuses on modernising the sector and helping companies move away from business as usual, investing in a sustainable, responsible and innovative way. © EBRD

During the Annual Meeting in Nicosia, the EBRD made a contribution to the local charity PeacePlayers Cyprus which promotes reconciliation and social inclusion across the island's communities through basketball. © EBRD

EBRD’s innovative Green Cities Programme, set up in 2016, provides a comprehensive business model for green urban development, combining strategic planning with investment and associated technical assistance. Green Cities is one way in which the EBRD is scaling up its green financing as a part of its Green Economy Transition (GET) approach.

Ulaanbaatar, Mongolia. In 2018, Ulaanbaatar was the first city in Asia to join the EBRD’s Green Cities. © EBRD

Under the Green Cities programme, these new electric buses in Batumi, Georgia will increase the reliability, safety and efficiency of public transport, while benefitting the environment by reducing emissions. © EBRD

In Skopje, North Macedonia, wastewater treatment has been identified as one of the most urgent tasks under the Green Cities Action Plan developed by the city authorities and the EBRD. © EBRD

The EBRD has been assisting Ukraine to address the challenge of making Chernobyl safe and secure since it was first invited by the country and the G7 to manage dedicated donor funds in 1995. © EBRD

In November 2016 the New Safe Confinement was moved over the old sarcophagus housing the destroyed reactor 4. © EBRD

The EBRD launched its first Economic Inclusion Strategy in 2017, to ensure that more sections of society - particularly women, the young and people living in remote areas - can benefit from economic progress.
© EBRD

Kozloduy nuclear power plant, Bulgaria. It is being decommissioned through the EBRD-managed Kozloduy International Decommissioning Support Fund (KIDSF). © EBRD

Qairokkum hydropower plant,Tajikistan. The EBRD's support to the rehabilitation of Qairokkum shows how climate resilience can be integrated into an infrastructure investment. © EBRD

The EBRD supports agriculture and food production projects in many countries like Kazakhstan, in line with the Bank's commitment to promote private sector participation in agribusiness. © EBRD

Salkhit wind farm, Mongolia. The first large-scale renewables project in Mongolia and the first new electricity generator in the country for the last 30 years. It was conceived by local investors with early EBRD equity participation. © EBRD

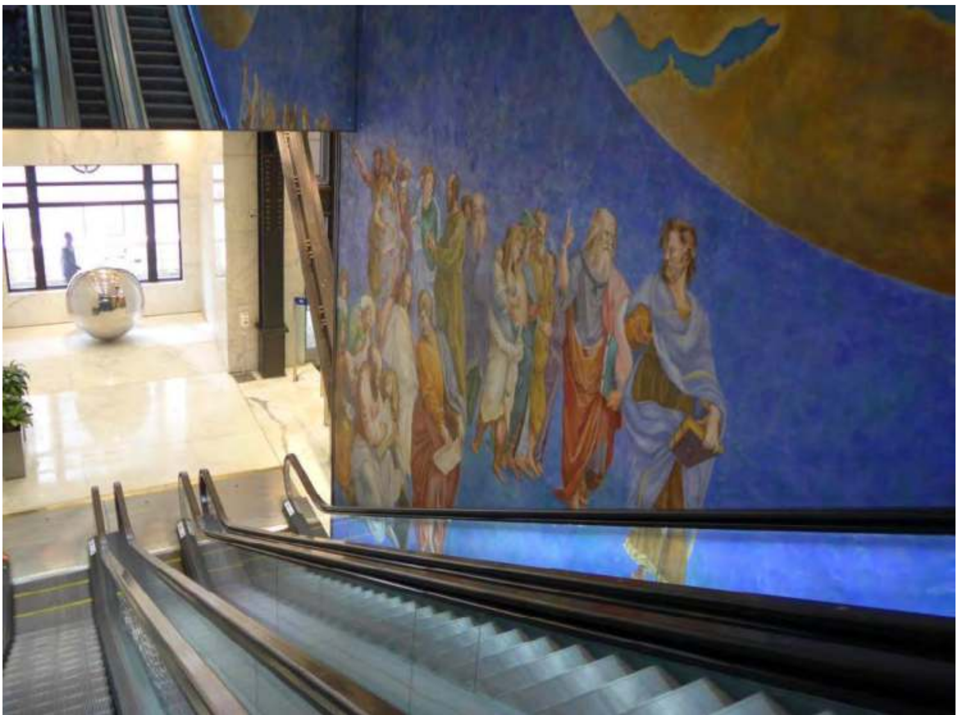
Khalladi wind farm, Morocco. Khalladi - the EBRD's first private renewable project in Morocco - will reduce greenhouse gas emissions by over 200,000 tonnes of CO_2 per year. © EBRD

Benban solar park, Egypt. The EBRD took a major step forward to support the rollout of renewable energy in Egypt in 2017 with the approval of a US$ 500 million framework to support the development of Benban, the largest solar park on the African continent. © EBRD

Croatia is taking a major step towards deepening its European integration with the completion of its part of the Pan-European Corridor Vc motorway, thanks to support provided by the EBRD. © EBRD

The EBRD Board of Governors approved the engagement of the Bank in the West Bank and Gaza in May 2017. The EBRD supports the development of the economy with investments channeled through a trust fund. Pictured here is Ramallah. © EBRD

Since 1992, the EBRD's Headquarters have been located in Exchange Square in the City of London. Shown here are the exterior of EBRD's Headquarters; its Bishopsgate entrance; and the Board Room. During the second half of 2022, the EBRD will move from Exchange Square to a new office at 5 Bank Street in Canary Wharf. © EBRD



Index

A

Ablyazov, Mukhtar 48
Aboulnaga, Fayza 43, 86–7, 96–7, 107
Acemoğlu, Daron 221
achievements of EBRD *see* contribution of EBRD; seven pillars of the EBRD
Acuner, Sevki 174–5
Advice for Small Business (ASB) programme 139, 141
African Development Bank (AfDB) 105, 365, 376
AfricInvest-TunInvest 109
agility of EBRD 409–11
Agreement Establishing the Bank (AEB)
  and extension of remit 103–4
  and financial markets 273–4
  and Iraq 118
  and political mandate 270
  and public infrastructure 202
  and Russia 182–3
  and transition concept 231, 233, 415
  and Turkey 25–9
Akfen Holdings 13
Albania 129, 159, 302, 307, 310–11
Algeria 104, 118
Allen, Mark 68
Almunia, Joaquin 351–2
Alpha Bank 129, 149, 290
aluminium industry 326–7
Anadolu Efes 13
Angelina, Pasha 243
Annual Meetings
  (2006) (London) 20–1, 346–8
  (2008) (Kyiv) 33–5, 43, 86–7
  (2009) (London) 71–3, 356
  (2010) (Zagreb) 88, 205, 356
  (2011) (Astana) 98–100
  (2012) (London) 107
  (2014) (Warsaw) 136–7, 261
  (2015) (Tbilisi) 180–1, 262–4
  (2016) (London) 181
  (2017) (Cyprus) 139–40, 182, 242
  (2018) (Jordan) 151
  (2020) (virtual) 118
Anthropocene 403
Arab Spring 43, 85–90, 91–8, 120–2
Armenia 183, 293, 310
Ashton, Catherine 92–4, 174
Asian Development Bank (ADB) 161, 318, 365, 376
assessment of transition challenges (ATCs) 212–13, 237
assessment of transition qualities (ATQs) 237–8
Association Agreements 171, 173
Azerbaijan 245, 338

B

Babacan, Ali 15, 17, 19, 37
Bahry, Donna 243
Bakradze, Davit 159
Bali Road Map 355
Balkans 12, 129, 130, 135, 261, 270
Baltic States *see also* Central Europe and the Baltics (CEB) 159, 279, 292–3
Ban Ki-moon 98, 365
Banca Transilvania 62
Bank Audi 117
Bank of Cyprus 138–9, 141
Bank of Georgia 62, 163

Bank of Greece 135
Bank TuranAlem 47–8, 52
bankers
  and economists 199–204, 217, 220
  and transition qualities 239
  uncertainties 200
Banking Department 57, 201–2, 216–17, 245–6, 419–20
banking sector
  in the Balkans 135
  in Cyprus 138–9
  in Egypt 114
  and foreign banks 52–3
  in Georgia 156, 160–3
  in Greece 128–9, 135, 149–50
  in Kazakhstan 47–52
  response to global financial crisis 62–3, 66–7
  in Russia 166
  in Turkey 258–61
  in Ukraine 191–3
Bankwatch 393
Barroso, José Manuel 96, 172
Bartzokas, Anthony 143–5, 153
Barysch, Katinka 125
Basel Institute of Governance 312
Basic Element 326–7
Bear Stearns 49
Belka, Marek 81
Ben Ali, Zine El Abidine 91, 113
Benn, Hilary 22, 351
Bennett, Phil 138
Berglof, Erik
  and the Besley Commission 208
  and coordination with other financial institutions 57
  and countries 'stuck' in transition 219–20
  departure of 226–7
  and the development model 281
  and global financial crisis 54–5, 66–7, 78, 80, 82–3
  and inclusion 251–2, 255–7
  and local finance 78, 284
  and Russia 179
  and south-eastern Europe recovery plan 132
  and transition impact 200, 203–4
  and Transition to Transition (T2T) 107
  view of EBRD contribution 431–3
Bergman, Michaela 251, 262, 263–4
Besley, Tim 208
Besley Commission 208–12, 214, 216, 221, 228–9
Besley II 229–33
'best available technology' (BAT) 214–15
Biden, Joe 375
Bielecki, Jan Krzysztof 107, 108
Bildt, Carl 173
Birol, Faith 387
Blair, Tony 22, 345–6
Blavatnik, Leonard 326
BMCE 113
Board of Directors
  and Cyprus 136
  and Gender Action Plan 249
  and Greece 147, 148–9, 151
  and partnership 419–20
  and renewable energy 392
  and Russia 165, 176, 180, 182
  and SEMED 109, 222
  and transition concept 232–3
  and Turkey 36
Board of Governors 100, 356
Bogolubov, Gennady 191
bonds
  corporate 153, 276–7, 294
  covered 289–90, 293
  EBRD 276, 293–4
  Eurobonds 113, 153, 156, 299
  government 126, 128
  green 290, 294–5, 379
  local currency 276–9, 282
  municipal 295, 296
Bouazizi, Mohamed 91, 120
Boyd-Carpenter, Harry 387, 388, 390, 391–2
Brock, Michelle 255, 256
Brown, Gordon 59, 73–4, 92
BTA Bank 47–8, 52
Buckley, Neil 133
Bulgaria 11, 129, 130, 159, 342–4
Bulgarian Energy Efficiency and Renewable Energy Credit Line Framework (BEERECL) 343–4
Bulgarian Post Bank 344
Bush, George W. 22–3, 73, 345
Business Advisory Services (BAS) 245
  Gender Action Plan (GAP) 253–4
Business Environment and Enterprise Performance Survey (BEEPS) 211, 270, 310

business model of EBRD 42–3, 400, 431–2, 435
business ombudsman
Business Ombudsman Council 311–13
Business Ombudsman Institution (BOI) 307, 311–15
in Kyrgyz Republic 314–15
in Ukraine 171, 185, 187, 192, 313

C

Canada 100
Canadian International Development Agency (CIDA) 245
Çanakçi, Ibrahim 18, 32, 34, 35
capital markets
and Covid-19 pandemic 300–1
development of 272–82
international 153
and transition 294–6
Capital Markets Development (CMD) 289, 300
capital of EBRD 62–3, 75–8, 408–9
Capital Resources Review (CRR)
fourth 71–3, 205, 291, 356
third 11, 346–8, 351
carbon reduction targets 357–9
carbon trading 351, 365–6
Carnaghan, Ellen 243
Central, Eastern and Southeastern Europe (CESEE) 57, 69, 71, 80–3
Central Asia 261, 370, 378, 421, 423–4
Central Bank of Israel 115
Central Bank of Russia (CBR) 316
Central Europe and the Baltics (CEB)
energy intensity 427–8
GDP growth 423
investment in 11
per capita income 421, 422*f*
structural reform 426
Centre for Global Development 322
Chakrabarti, Suma
and capital markets 273
and Cyprus 139
and the EBRD 407
and Egypt 109–10
election to EBRD Presidency 108
and eurozone crisis 132–6
and Gender Strategy 251, 252, 263
and GET 373–5
and good governance 271, 306, 307
and Greece 130, 131, 151–2
and inclusion 265–6
and Investment Councils 308–9
and Lebanon 117
and modernisation of the EBRD 215–17
and One Planet Summit 385–6
and Paris Agreement 376
and policy reform and engagement 184, 225, 319
replacement of 120
and Russia 166, 178, 180, 183–4
and transition 220, 227–8, 230, 239
and Tunisia 114
and Ukraine 169–70, 171–2, 180, 184–7, 191–2
challenges for EBRD 403–4
Charles, Jonathan 182, 220
Chirac, Jacques 18
Cigna, Gian Piero 327, 328, 332, 334
Citadele 65
Clark, Alistair 264
Clausewitz, Carl von 439
Clean Technology Fund 389
Client Services Group (CSG) 217
CLIMADAPT 378–9
climate adaptation 378–9
climate change
and Copenhagen COP15 364–6
and EBRD role 231, 337–8, 438–9
and Gleneagles Summit 345–6
and Green Cities Framework 382–4
and halting of coal and oil investment 392–4
interest in 214–15
interventions in 358–63
and a majority 'Green' bank 394–400
and One Planet Summit 385–6
and Paris Agreement 375–9, 385
ready to counter threats of 405
and renewable energy 386–92
systemic approach to 396
and transition 363–4
Climate Change and Energy Efficiency Initiative 348, 350
Climate Investment Funds (CIFs) 362–3
climate resilience 378–9
climate resilience bond 379
CO2 emissions
challenge of increase in 403

in Cyprus 141
in Poland 294
reduction in 203, 214, 357, 366–7, 380–1
coal-powered energy 392–4
competitiveness 233, 234
Conference of the Parties (COP)
COP1 337–8
COP13 355
COP15 364–6, 375
COP16 365
COP21 372–3, 375, 382
COP26 397
conflict
in Georgia 55, 62, 155–64
historical 438
impact of 438
in Syria 116
in Ukraine 165, 174, 187
contagion 52–5
contribution of EBRD 428–35
coordination
of IFIs 57–60, 73, 102, 105
and multilateral solutions 435–8
and Vienna Initiative 58, 66–71, 79–82, 272, 285–6, 324
Copenhagen Accord 364–6, 372
corporate bonds 153, 276–7, 294
corporate governance 303, 325–34
Corporate Governance Action Plans (CGAPs) 329–30, 333–4
'Corporate Governance Approach Statement by DFIs, A' 328
Corporate Governance Development Framework 328
Corporate Governance Reviews 329–30
corruption
and anti-corruption efforts 169–72, 320–2
in countries of operation 228–9
deep and persistent 167–72
following global financial crisis 197, 204
in Georgia 158
at Naftogaz 331
and private sector 270–1
in Russia 166
in Ukraine 168–72, 175, 186
Council of Europe 29
Country and Sector Economics (CSE) 217
Country Economics and Policy (CEP) 224–5
country strategies 224–5
Coutanche, Hester 309–10
covered bonds 289–90, 293
Covid-19 pandemic
and capital markets support for recovery 300–1
challenge of 403
and demand for finance 274
and GET2.1 398–400
and inclusion 267
Local Currency Lending Facility 289
and requests for support 406–7
Crimea 165, 175, 187
critical mass 200–1
Croatia 159, 295, 296
Currency Exchange Fund (TCX) 288
Cyprus
achievements in 140–2
banking sector 138–9
as country of operations 123, 136–42
economic recession 129
and the eurozone 126–7
GDP growth 127
per capita GDP 124
relationship with EBRD 138–9
and Turkey's accession to EU 10, 17–18
unification hopes 137, 139–40, 141–2
Czech Republic 36, 62, 159, 407

D

Davey, Mike 40–1, 255
Davis, Mark 293
de Larosière, Jacques 339, 429
Deauville Partnership 101–2, 105–6
Deauville Summit Declaration 101–2
debt of EBRD 408–9
debt relief for poorest countries 345
debt restructuring 323–5
debt to GDP ratio 126
decarbonisation 141, 294, 372, 392–4
Deep and Comprehensive Free Trade Area (DCFTA) 171, 173
Delević, Milica 304, 305, 310
Đelić, Božidar, 108
Della Rosa, Valeria 258–9
Demchenko, Maria 243
Demiralp, Oğuz 10
democracy 198, 209, 219, 416
Dendias, Nikolaos 143
Deripaska, Oleg 326

derivatives 293–4
Derviş, Kemal 15
Descamps, Olivier 258
DESFA 150
development finance institutions (DFIs) 328–9, 362
development models 281–2
Dewatripont, Matthias 208, 230
digital transition 319
district heating 340–1
Doukas, Alex 393
Dragasakis, Yannis 150–1
Dziurman, Sabina 65, 140–1, 149–50, 152–3

E

Early Transition Countries (ETCs) 286–8
  Local Currency Risk Sharing Special Fund 287
Early Transition Countries Initiative (ETCI) 261
  and Investment Councils 308
  Local Currency Loan Programme 287–8
Eastern Europe and the Caucasus (EEC) 423
Eastern Europe Energy Efficiency and Environment Partnership (E5P) 363
Eastern Partnership (EaP) 171, 172, 261
EBRD bonds 276, 293–4
EBRD-Ukraine Stabilisation and Sustainable Growth Multi-Donor Account 313
Economic and Financial Affairs Council (ECOFIN) 24, 31
economic growth 53–5, 404
Economic Inclusion Strategy 242, 264–7
economists
  and bankers 199–204, 217, 220
  and environmentalists 214
  major influence of 199–200
  role of in response to global financial crisis 58
effective markets 269–71
Egypt
  agreement on 95–6
  Cairo Overnight Interbank Average (CONIA) 299
  as choice for potential expansion 13
  as country of operations 86–8, 90, 92–4
  diagnostic study 225
  financial support 94–5
  first projects 106, 110
  GDP growth 121*t*
  included in SEMED 104
  investment in 114–15, 122*t*, 167
  and Israel 96–7
  private/public sector spending 120
  protests 91–2
  regional offices 112, 119
  renewable energy 391–2
  as shareholders in EBRD 106
  solar power 120, 391–2
  Transition-to-Transition (T2T) events 107
  uncertainty 109–10
  Women in Business programme 261
Eichenberger, Joe 428–30
electricity supply 113
'elephant chart' 241–2
Emerging Europe and Central Asia 421, 422*f*
endorsement for EBRD activities 105–6
energy efficiency
  and carbon reduction targets 357–9
  efforts to improve 338–44
  and energy audits 341
  and energy intensity 426–8
  focus on 337
  grants and subsidies for 359–63
  in industry and infrastructure sectors 341–2
  investment in 112–13
  and sustainable energy business model 346–9
  Sustainable Energy Initiative (SEI) 349–57
Energy Efficiency and Climate Change (E2C2) team 348–9, 357
energy efficiency team 339, 341
Energy Group 339
Energy Operations Policy 338
energy performance contracting (EPC) 340
energy sector 188–91
energy security 355
energy service companies (ESCOs) 339–41
Enerjisa Enerji 295
Environmental and Social Policy (ESP) 246, 248
environmental issues 202–4, 213–15
Environmental Policy 244, 246
environmental sustainability 233, 235
environmentalists 200, 202–4, 214

equal opportunities 241–2, 405
Erdoğan, Recep Tayyip 9, 17, 22
Estonia 52
Eurasian Economic Union 173
euro 283
Eurobank 129, 149
Eurobonds 113, 153, 156, 299
Eurogroup 142–3
Europe *see* southern and eastern Mediterranean (SEMED)
European Bank Coordination Initiative *see* Vienna Initiative
European Central Bank (ECB) 125–6, 149
European Commission
  and Georgian conflict 161
  and halt to financing in Russia 178–9
  'Roadmap to a Resource-Efficient Europe' 370
  Task Force for Greece 143
  view on Turkey becoming recipient country 24
European Council 9, 10, 29, 185
European Economic Community (EEC) 8–10
European Investment Bank (EIB)
  and Egypt 93
  and extension of remit 100
  and framework for cooperation 95–6
  and Georgian conflict 161
  and Greece 144
  and Turkey 15
  and Ukraine 186
  and Vienna Initiative 2.0 81
  view on Turkey as recipient country 24
European Union (EU)
  and Eurozone crisis 142
  and extension of remit 100
  on Georgian conflict 160
  and halt to financing in Russia 175–6, 178
  Neighbourhood Investment Facility (EU-NIF) 261
  policy and the EBRD 144–5
  position on Arab Spring 96
  role in policy formulation 56
  as shareholders 418–19
  structural funds 80
  and suspension of Ukraine talks 172–4
  Task Force in Greece 135
  and tensions between Russia and Ukraine 165
  and Turkey 8–10, 42
  and Ukraine 171
  view on Egypt as country of operation 92–4
  Women in Business programme 258–9
European-Mediterranean (EuroMed) Bank 88–90, 94–6
eurozone 123–7, 144
Evaluation Department (EvD) 311, 314, 324–5, 354, 357–8, 428
expected transition impact (ETI) 222–4
external perspectives on EBRD contribution 433–5

F

Fabius, Laurent 375
Fattah el-Sisi, Abdel 110
'Fighting the Crisis, Promoting Recovery and Deepening Transition' 72, 205–6
financial institutions 62–3
Financial Institutions (FI) team 246, 342
financial integration 82–3, 281
financial markets 78–9, 272–8, 291–2, 292*f*
financial markets development index 300
financial results of EBRD 180
financial sector 47–52, 114, 149–50, 153
Financial Stability Board (FSB) 323
Finansbank 261
First Vice President (FVP) 419–20
Fischer, Jan 107
FMO 328
Fontaine Vive Curtaz, Philippe de 89, 94, 108
foreign banks 52–3, 66–70
foreign currency 272, 274–5, 276, 279–82
foreign direct investment (FDI) 46, 78, 130, 156, 161
'Fostering Economic Inclusion with the Transition Impact Methodology' 257
France 88–90, 99, 107–8
Freeman, Ron 429
Freeman, Varel 61, 64, 354
Frontclear 298
Full Forums 70, 79, 80, 285

G

G7 (Group of Seven) 73, 157, 372
G8 (Group of Eight) 101–2, 105, 338, 345–7, 350–2, 369

G8 Gleneagles Plan of Action on Climate Change, Clean Energy and Sustainable Development 346
G20 (Group of 20) 73–5
  Making the Global Financial System Work for All 435
Gacek, Hildegard 111–14
Gaddafi, Muammar 106
Garanti Bankasi 254, 261
gas sector 188–91, 331–4, 393–4
'gas wars' 172–3
Gažić, Ivana 296
GCF-EBRD SEFF Co-financing Programme 379–80
GDP growth 45–6, 71, 121*t*, 423–4, 424*f*, 425, 425f
Geiger, Kurt 48
Geithner, Timothy 99
'Gender - Time for a Strategy' 251
Gender Action Plan (GAP) 246–50, 252
Gender and Economic Inclusion team 266
gender awareness campaigns 248
gender equality 231, 243–6, 262–4
Gender Action Plan (GAP) 246–50
Gender Equality Strategy 262–4
Gender Equality Study 245–6
  gender issues 222, 243–4, 244–6, 250
  Gender Strategy 251–5
  Gender team 246, 249
geopolitical tensions 155–6
Georgia
  banking sector 156, 160–3
  conflict 55, 62, 155–64
  corruption 158
  derivatives 293
  financial support 62
  foreign direct investment (FDI) 156, 161
  GDP growth 157
  gender equality pilot projects 248–9
  good governance 302
  impact of conflict on economy 160–1
  infrastructure 161–2
  Investment Council 310
  local capital markets 293–4
  and NATO 158–9
  PPPs 318
  Tbilisi Inter Bank Rate (TIBR) 299
Georgiades, Harris 136, 138, 139
Georgieva, Kristalina 434
Germany 89–90, 99, 107, 338
Gheorge, Mariana 253
Giscard d'Estaing, Valéry 9
Gleneagles (G8) Summit 345–7, 350, 351–2
Global Environment Facility (GEF) 363
global financial crisis
  and capital increase 75–8
  and contagion 52–5
  and energy efficiency 354–5
  and graduation 36, 41–2
  in Kazakhstan 47–52
  and Legal Transition Programme (LTP) 318–19
  and local finance 78–9
  and markets 45–6
  and reliance on foreign currency 281
  response to 56–63, 71–5
  and transition 82–4, 197, 204–5
  and Vienna Initiative 66–71
  and 'Vienna Plus' 79–82
global warming 337–8, 378–9, 403
globalisation 241–2, 438
goals and objectives of EBRD 404–7
Gontareva, Valeria 191–2
good governance
  and economic performance 301–4, 302f
  importance of 220
  at the national level 305–15
  successful improvement of 334–6
  support for 269–73
  system for 209
  as transition quality 233, 234
Governance and Political Affairs (GPA) team 271
governance of EBRD 107–8
government bonds 126, 128
graduation from EBRD 11–14, 20, 61–2
Gramegna, Pierre 182
grants and subsidies 359–63
Greece
  achievements in 152–4
  anti-austerity 148
  assessment of 145–6, 149–50
  banking sector 69, 128–9, 135, 149–50
  controversy over 144–5
  as country of operations 123–4, 134–5, 142–5, 146–8
  crisis 80, 128–9
  debt to GDP ratio 126

election results 147–8
and the eurozone 125–7
extended mandate for 150–4
financial sector 149–50, 153
government deficit 125–6
green bond issue 294
household income 127
investment in 128–9, 146, 148–50, 153–4
per capita GDP 124
period of volatility 148
private sector 150, 154
privatisations 150
relationship with 129–31
as source of FDI 130
support for 131–4
unemployment 127
Greek Institution for Growth 134
Green and Sustainability Bond investment framework 290
'Green' bank 394–400
green bonds 290, 294–5, 379
Green Cities Framework 382–4
Green Cities Network 383
Green City Action Plans (GCAPs) 382–3
Green Climate Fund (GCF) 365, 378, 379–80, 384
Green Economy and Climate Action 387
Green Economy Financing Facilities (GEFFs) 369, 379–82
Green Economy Transition (GET) 215, 369, 372–7, 379–80, 386, 395–400
green finance 338, 372, 395–400
Green Technology Selector 381
greenhouse gases (GHGs) 340, 345, 350, 354, 357–9, 372, 396, 427–8, 427*f*
Guidelines on concessional finance 361–2
Gurgenidze, Lado 158, 161, 163
Guriev, Sergei 208, 210, 227, 230, 242, 432
Guterres, Antonio 385, 395
Gyurcsány, Ferenc 61

H

Hansen, Catarina Bjorlin 161–2, 163
Harmgart, Heike 119–20
Hatzidakis, Kostas 130, 135, 143
Heilbronn, Pierre 226
Hellenic Bank 139
High Level Reporting Mechanism (HLRM) 312
High-Level Advisory Group on Climate Financing (AGF) 365
Hollande, Francois 372
Honeywell 340
Host Country Agreements 112
Hourican, John 138
Hungary 66, 159, 276, 279–81, 338
Hydro-OGK 278

I

inclusion
and Covid-19 pandemic 267
and the EBRD 242–3
economic inclusion strategy 264–7
impact of lack of 229
importance of 220
promotion of concept of 252
and refugees 265
and transition 255–7
and transition impact methodology 221–2
as transition quality 233, 235
incomes per capita 403–4, 421–2, 422*f*
industry sector 341–2
inequality 241–2, 404
informal sector 250
Information Session 248
infrastructure sector 201–2, 341–2
insolvency 323–5
Insolvency and Creditor Rights (ICR) Standard 323
institutions 229, 269–71
integrated approach 211–12, 233, 236
Intergovernmental Panel on Climate Change (IPCC) 337–8, 364, 394–5
International Capital Market Association (ICMA), Green Bond Principles 294
international capital markets 153
International Development Law Organisation (IDLO) 317
International Energy Agency (IEA) 350
World Energy Report 387
International Finance Corporation (IFC) 15, 161, 163, 225, 326–8
international financial institutions (IFIs) *see also* Joint IFI Action Plan (JIAP); Vienna Initiative 73–4, 105–6
International Monetary Fund (IMF)
and experience in economic crises 56
and Georgian conflict 161

and Parex Banka rescue 63
and Turkey 15, 17
in Ukraine 186, 189–90
and Vienna Initiative 68
International Renewable Energy Agency (IRENA) 387
International Swaps and Derivatives Association (ISDA) 293
International Women's Day 244
InvestBank 109
investment
in CEB 11
and corporate governance 326–7
in Egypt 114–15, 122*t*, 167
in energy efficiency 112–13
in Greece 128–9, 146, 148–50, 153–4
halting of coal and oil 392–4
from IFIs 81
in Jordan 112–13, 122*t*
in Kazakhstan 46–7
in Lebanon 122*t*
in Morocco 113, 122*t*
in North Africa 102
and policy reform and engagement 184, 414–15
rankings of EBRD 115
in region 60
rise in 63
in Russia 12, 41–2, 165–7, 177
in SEMED region 105–6, 111–12, 118, 122*t*
in Serbia 129
in Tunisia 113–14, 122*t*
in Turkey 41–3, 167
in Ukraine 184–7
in West Bank and Gaza 122*t*
Investment Climate and Governance Initiative (ICGI) 306–11
Investment Councils (ICs) 307, 308–11
Iraq 13, 104, 118, 437–8
Ireland 80
İşbank 255, 261
Islamic Development Bank (IsDB) 105
Israel 96–7
Italy 99, 183, 309

J

Japan 29, 37, 99
Javorcik, Beata 230, 301, 432
Joint IFI Action Plan (JIAP) 70–1, 81, 133, 134
Joint Needs Assessment (JNA) 161–2
Jollands, Nigel 383, 384
Jordan
applications for EBRD funding 103
first projects 109
GDP growth 121*t*
included in SEMED 104
investment in 112–13, 122*t*
regional boundaries 104
regional offices 112
renewable energy 390–1
as shareholders 106
solar power 390–1
and Syrian refugees 265
thermal power 390–1
tourism support 120
unemployment 250
Journal of Labor Economics (JOLE) 244
Just Transition Initiative 294
Justice and Development Party (AKP) 9

K

Kaberuka, Donald P. 227
Karacadag-Sundararjan-Elliott Model 292f
Karimov, Islam 170
Kazakhstan
banking sector 47–9
diagnostic study 225
economic recovery 128
Eurasian and Economic Union 173
financial problems 46–52
financial sector 47–9
foreign direct investment (FDI) 46
GDP growth 52
investment in 46–7
KazPrime 279
loan-to-deposit ratios 49
and Paris Agreement 377–8
renewable energy 389
solar power 389
TONIA 299
visit from President 62
Kazkommerzbank (KKB) 47–8, 52
KazPrime 279
Khanjenkova, Natasha 177
KievPrime 279
Kim, Jim Yong 375–6, 385
knowledge creation 229
Kolomoisky, Igor 191

Kosovo 131, 158–9, 377
Kotova, Elena 23
Kozloduy International Decommissioning Support Fund (KIDSF) 343
Krkoška, Libor 139
Kubas, Jacek 289, 296
Kuno, Chikako 246
Küüsvek, André 47–8, 51, 291
Kyoto Protocol 345
Kyrgyz Republic 45, 183, 248–50, 287, 314–15, 316–17

L

labour productivity 423
Lagarde, Christine 77, 434
Lankes, Hans Peter 59, 90, 200, 203–4, 227–33, 239
Larosière, Jacques de 339, 429
Latvia 62, 63–5, 66, 69
Law and Justice (PiS) party 389
Le Houérou, Philippe 224, 225–6, 239
Lebanon 104, 116–18, 121*t*, 122*t*
legal and regulatory framework 289–96
legal reforms 315–25
legal team 335
Legal Transition Programme 318–19
Legal Transition Team (LTT) *see also* Vienna Initiative 202, 271, 289, 315–19, 323–5, 329–31
Lehman Brothers 39, 51, 53, 55, 128, 163
Lemierre, Jean
  and corporate governance 328
  and CRR3 346
  and G8 347–8
  and graduation 11
  on SEI 352
  and Turkey 14, 20, 31, 35, 36–7, 39
Libya 104, 105–6, 118
Life in Transition Survey III 127
Life in Transition Survey (LITS) 204, 211, 255
loan-to-deposit ratios (LDRs) 49, 69
local currency and capital markets 78–9, 153, 272–3, 276–9, 282–300
Local Currency and Local Capital Markets Development (LC2) initiative 78–9, 273, 282–300
  LC2 Development Strategic Initiative 291
local currency bonds 275–9, 282
local currency finance 78–9, 114, 288–9, 297–8
Local Currency Lending Facility 288–9
local manufacturing 114
local presence of EBRD 412–13
London Stock Exchange 277
losses 55, 180
Loudyi, Abdeltif 88
low-carbon transition 213–15, 372
Luxembourg 261

M

Macedonia, Former Yugoslav Republic of 159, 296
Macron, Emmanuel 385
Maidan Revolution 174–5
'Make Poverty History' campaign 345
Malaysian airliner (MH17) shooting 165
Malige, Francis 189, 190, 192–3, 254, 259
Malta 126
management of EBRD 11–24, 25–30, 216
Marchand, Luc 50
market economics
  balancing of 204–11
  crisis in 45–6
  development of 297–9
  different conceptions of 418–19
  effective 269–71
  ensuring well-functioning 405
  lack of inclusion undermines 229
  lack of social cohesion undermines 229
  qualities of sustainable 232–9
  reforms 219–20
  and revision of transition concept 231–2
Massimov, Karim 50
materials efficiency 371
Maurice, Emmanuel 315
Maystadt, Philippe 24, 95–6
McCallion, Terry 342
McCormick, David 33, 34–5
McGillivray, Gavin 34
McKinsey 355–6
Mebonia, Levan 434
Mediterranean region *see* southern and eastern Mediterranean (SEMED)
Medvedev, Dmitry 160, 168
Memorandum of Understanding (MoU) 95–6, 105, 287, 292, 307, 310–11
Merkel, Angela 18, 190, 372

Mezouar, Salaheddine 98
Middle East and North Africa (MENA) 86, 98–9, 118
MidSEFF 369
Milanović, Branko 241–2
Milhaud, Charles 88–9
Millennium Development Goals (MDGs) 238, 246, 370
Milushev, Nik 232
Ministry of Foreign Affairs (MFA) (Turkey) 17
Ministry of Labour and Security (Turkey) 258
Ministry of Treasury and Finance (Turkey) 42–3, 435
Minsk Protocol 187
Mirow, Thomas
  and capital increase 76–7
  and Egypt 88, 92–3, 94–6, 97
  and EuroMed initiative 90
  and extension of remit 98–9
  'Fighting the Crisis, Promoting Recovery and Deepening Transition' 205
  and gender issues 248
  and global financial crisis 55–6, 60, 72–3
  and Kazakhstan 62
  and MDGs 246
  and 'New Growth Agenda' 78
  replacement of 107–8
  and role of EBRD 58–9
  and SEMED 106
  and Turkey 39
modernisation of the EBRD 215–26
Moldova, Green Cities Framework 384
Molterer, Wilhelm 34
Money Market Working Groups (MMWGs) 298
money markets 278–9, 298–9
Mongolia
  as country of operations 26, 28
  membership of EBRD 8
  and non-EBRD funding 131
  and Paris Agreement 378
  as precedent for geographical remit 103
  renewable energy 388
  sided with Russia 183
  wind power 388
Monitoring, Reporting and Verification (MRV) system 359
Moody's 49
Morocco
  as country of operations 88, 97–8
  first projects 109
  GDP growth 121*t*
  included in SEMED 104
  investment in 113, 122*t*
  MONIA 299
  regional offices 112, 119
Morsi, Mohamed 109–10
Mosenergo 278
MosPrime (Moscow Prime Offered Rate) 278–9
Mubarak, Hosni 91–2, 109
multilateral development banks (MDBs) 58, 74–5, 376, 436–7
municipal bonds 295, 296
Muslim Brotherhood 110

N

Naftogaz 188–92, 331–4
Nagy-Mohácsi, Piroska 57, 66, 285
Narmania, Davit 383–4
National Bank of Egypt 114
National Bank of Greece (NBG) 129, 149, 294, 434
National Currency Association 278
Nationally Determined Contributions (NDCs) 375, 377
Nazarbayev, Nursultan 48, 50–1
'Neocon' agenda 21
Netherlands 23–4
new era for EBRD 438–9
non-EBRD funding 131
non-performing loans (NPLs) 324–5
North Africa *see* southern and eastern Mediterranean (SEMED)
North Atlantic Treaty Organization (NATO) 37, 158–9
North Korea 37
Norway 35
Nuland, Victoria 186
Nussbaumer, Michel 316, 325

O

Obama, Barack 92, 98–9, 110, 375
Office of the Chief Compliance Officer (OCCO) 305
Office of the Chief Economist (OCE) 19, 57–8, 200–2, 211, 217–18, 271, 361, 431–3

Office of the General Counsel (OGC) 19, 315
O'Grady, Lin 383–4
OGResearch 298
oil, halting of investment in 393
Oil Change International 393
One Planet Summit 385–6
open economy 405
openDemocracy website 169
Operational Effectiveness and Efficiency (OE&E) 217
Operations Committee (OpsCom) 218
Orbán, Viktor 280
Ord-Smith, Robin 314
Oreshkin, Maxim 182–3
Organisation for Economic Corporation and Development (OECD) 312
  Principles and Guidelines for Corporate Governance of State-Owned Enterprises 333–4
  Principles of Corporate Governance 328–9
Organisation for Security and Cooperation in Europe (OSCE), Minsk Protocol 187
Osborne, George 108
Oxford International Relations Society 94
Oxford University 94
Oz, Turan 24

P

Pacatte, Aude 297–8
Pak, Oksana 254
Palestinian Authority 115
Parex Banka 62, 63–5
Paris Agreement 375–9, 385, 397, 400, 436
Paris Club 57, 67
Parshad, Nandita 393–4, 399–400
partner financial institutions (PFIs) 260
partnerships of EBRD 418–20
Paulson, Henry 73
peace dividend 179
Peace Players Cyprus 140
Peskov, Dmitry 174
Petrom 253
Pilloux, Alain 226, 430–1
Piraeus Bank 129, 149
Pivovarsky, Alexander 300
PKO Bank Hipoteczny 290
Plekhanov, Alex 232
Počiatek, Jan 87–8
Poland 11, 159, 290, 294–5, 389–90, 421
policy reform and engagement 184, 225–6, 414–15
political mandate of EBRD 270, 416–18
population of EBRD region 155, 403–4
populism 242
Poroshenko, Petro 187
Portugal 80
poverty reduction 403
Power Purchase Agreement (PPA) 392
principles and practice of EBRD 404–7
Priority Policy Objectives (PPOs) 319
PrivatBank 191–3
private sector
  blocks to development of 270–1
  focus on 121
  in Greece 150, 154
  leading EBRD 411–12
  and public sector partnership 419–20
  in Russia 166
private sector finance 436–7
private sector participation (PSP) 227–8
privatisations 150, 209, 228
productivity 422–3
'productivity catch-up' 218–19
professional managers 303
profitability 55
profitability of EBRD 408–9
progress in EBRD region 421–8
Project Christopher 236–7
Project Monarch 237
ProZorro 319–22
public sector 419–20
public-private partnerships (PPPs) 225, 317–18
Putin, Vladimir 175
Pyatt, Geoffrey 186

Q

qualities *see* transition qualities

R

Radonjic Ker-Lindsay, Biljana 248–9, 251
Radziwill, Artur 224
Raiffeisen Bank International 69
Rama, Edi 307, 310
Rambousek, Barbara 251–2, 255–7, 264, 266–7
ratings agencies 163
ratings of EBRD 408–9

'Reduce, Reuse, and Recycle (3R) Initiative' 369
refugees 116–17, 264–7
regional offices 119, 139–40, 413
regulatory framework 289–96
Rehn, Olli 95
Reichenbach, Horst 19, 95, 131, 248
Reiner, Bojana 188
Reiserer, Axel 94
remit of EBRD 98–107
Renaud-Basso, Odile 120–1, 400
renewable energy 113, 114, 141, 386–92
repeat clients 200–1
resilience
  climate 378–9
  strengthening economic 272–82
  successful improvement of 335–6
  support for 269–73
  for sustainable economy 405
  as transition quality 233, 235
resource efficiency 367, 369–71
results reporting 216
Results Task Force 221
Reverta 65
Revolution of Dignity 174, 306–7
Rice, Condoleezza 22, 37
Ripplewood Advisors 65
Risk Loss Cover (RLC) 259–60
'risk-free rates' (RFRs) 299
Robinson, James 221
Rodina, Anastasia 314
ROISfix 299
role of EBRD 56–9, 404–7
Romani, Mattia 226, 237, 399
Romania
  banking sector 129
  Bucharest stock exchange 296
  covered bonds 290
  financial sector 135
  Gender Action Plan (GAP) 253
  gender equality pilot projects 248–9
  good governance 303
  investment in 11
  municipal bonds 295
  and NATO 159
  as source of FDI 130
Roth, Wolfgang 24
Rouble Overnight Index Average (RUONIA) 299
Ruhe, Charlotte 261
Rusal 326–7
Russia
  aluminium industry 326–7
  annexation of Crimea 165, 187
  banking sector 166
  and ceasing of new EBRD finance 41–2, 164–5, 175–84
  and conflict in Georgia 160–2
  continuing role at EBRD 156
  corporate governance 326–7
  Corporate Governance Code 316
  disputes with Board 155
  Economic Development Ministry 178
  economic recovery 128
  energy intensity 350, 427
  Eurasian Economic Union 173
  and extension of remit 100
  'gas wars' 172–3
  GDP growth 423–4
  importance to EBRD 165–7
  investment in 12, 165–7, 177
  legal arguments 181–3
  local currency and capital market development 278–9
  MICEX-RTS stock exchange 295
  Minsk Protocol 187
  MosPrime (Moscow Prime Offered Rate) 278–9
  private sector 166
  relationship with USA 22–3
  reliance on 12
  Rouble Overnight Index Average (RUONIA) 299
  share of bank business 155–6
  staff numbers in 177
  stagnation of economy 179–80
  and Turkey 23
  and Ukraine 164–7, 168, 172–3
  use of foreign currency 275

S

Saakashvili, Mikheil 156, 158, 160, 169
Sarkozy, Nicolas 73, 88, 94, 101, 160
Sea Island (G8) Summit 369
sector expertise of EBRD 413–14
Securities Market Law (2003) 278
Seker Bank 255, 261
Šemeta, Algirdas 187, 313

Serbia 129, 135, 158–9, 212, 302
seven pillars of the EBRD 407–16
Shareholder Special Fund (SSF) 115, 318
shareholders of EBRD 7–8, 20–5, 31, 77, 98–100, 183–4, 418–19
Shevardnadze, Eduard 158
Siberian-Urals Aluminium Company (SUAL) 326–7
Şişecam 13, 371
Skrekas, Kostas 146–7
Slovak Republic 159, 316
Slovenia 159
small and medium-sized enterprises (SMEs) 114, 141, 288–9, 296
SME Local Currency Programme 288
Smith, Ian 380–2
social cohesion 209, 229
social standards 202–4
Société Générale 69
Société Générale Marocaine de Banques 109
solar power 120, 387
Soros, George 331
South Korea 37
southern and eastern Mediterranean (SEMED)
  action plans 131–4
  applications for EBRD funding 102–4
  applications for EBRD membership 102–4
  building up operations in 107–19
  difference to former Soviet Union countries 111–12
  energy intensity 427
  and extension of remit 98–107
  GDP growth 121*t*, 124, 423, 424
  gender issues 250
  impact of EBRD engagement 119–20
  inclusion 222
  investment in 102, 105–6, 111–12, 118, 122*t*
  non-EBRD funding 131
  and Paris Agreement 378
  per capita income 421–2, 422*f*
  problems in 128–9
  regional boundaries 104–5
  regional offices 119
  renewable energy 386
  Special fund 109–10
  ten years after 119–22
  Transition-to-Transition (T2T) events 107
  unemployment 250
  women in 250
  Women in Business programme 261–2
sovereign lending 201–2, 225
Soviet Union 111–12, 243–4
Spain 80
Special Climate Change Fund (SCCF) 363
Special Funds 93, 103–4, 109–10
Special Shareholders' Fund (SSF) 361
Stabilisation and Sustainable Growth Multi-Donor Account (MDA) Fund 186–7
Stakhanov, Alexei 243
Standard and Poor's 50, 163
standards of living 404
Stand-By Agreement 161
star projects 237
state role 405
state-owned enterprises (SoEs) 201–2, 303–4, 330–1
STEM disciplines 244
Stern, Nick 214, 353, 366, 377, 431–3
Stern Review 353
stock exchanges 295–6
Stoltenberg, Jens 365
Stop Funding Fossils 393
Storchak, Sergei 180–1
Strategic and Capital Framework (SCF)
  2016–2020 226, 262
  2021–2025 118, 396, 437
Strategic Gender Initiative (SGI) 252–5
Strategy and Policy Committee (SPCom) 216–17
Strategy for Local Currency and Capital Markets Development 273
Strategy for the Promotion of Gender Equality 262–4
Strizovic, Svetlana 435
structural reform 426, 426f
sub-Saharan Africa 437–8
success of EBRD 11, 45–6
Sullivan, Mark 21
Sustainable Development Goals (SDGs) 227–8, 238–9, 263, 370, 372, 404
sustainable energy 203
sustainable energy business model 346–9
Sustainable Energy Financing Facilities (SEFFs) 342–4, 356, 360, 366, 368–9, 379–80
Sustainable Energy Index 211
Sustainable Energy Initiative (SEI) 213–14, 349–57, 357–9, 362–3, 366–7

Sustainable Resource Initiative (SRI) 366–71
Swedbank 63
Swedish International Development Cooperation Agency (SIDA) 258
  Women in Business programme 261
Święcicki, Marcin 313
Syria 104, 116–17, 118, 265
Syriza political party 148
systemic approach of the EBRD 415–16

T

Tajikistan 287, 308, 378–9
Tanaka, Josué 347–8, 350, 354, 382, 396, 398
task forces 61, 131, 134, 216, 367
Tatishev, Yerzhan 48
Tauron group 294–5
TAV 13
Taylor, John 315
TBC Bank 62, 163
Tereshkova, Valentina 243–4
terrorism 345
Tesseyman, Nick 62, 149, 162
Thunberg, Greta 395
total factor productivity (TFP) 422–3
tourism 120, 161
Trade Facilitation Programme (TFP) 61, 141
Trans Adriatic Pipeline 135
transition
  and Besley Commission 208–11
  and capital markets innovations 294–6
  and climate change 363–4
  debate on the meaning of 7–8
  deepening 205–7
  development model 82–4
  and expected transition impact (ETI) 222–4
  goal of 404–5
  graduation from 11–14, 20
  and inclusion 255–7
  incremental methodological improvements 211–15
  Integrated Approach (IA) 211–12
  low-carbon 213–15
  methodological strains 199–204
  negative impact on women 247
  rethinking 197–9, 204–5
  'stuck in' 218–21
  task forces on 216
transition concept
  Besley II 231–2
  and operationalisng the changes 236–9
  Transition Concept Review 225, 226–36, 233, 236–7, 239–40, 264
transition impact
  of EBRD region 421–8
  and environmental issues 214–15
  and expected transition impact (ETI) 222–4
  and inclusion 221–2, 256–7
  methodology 221–2, 405–6
  transition impact assessment system 200
transition indicators 206, 206*f*, 210–11, 212–13
transition qualities 207, 237–8, 305–6, 405
Transition Reports 206–7, 213, 229, 426
  (1994) 210
  (2008) 54
  (2009) 83, 207, 281–2
  (2010) 280
  (2013) 218–21, 256, 305, 306
  (2016) 241–2
  (2017) 265
  (2019) 301
Transition-to-Transition (T2T) 107
transitory nature of EBRD 21–2
Transparency International 312, 320, 322
transport sector 120, 186
Treasury 297–9
Treichl, Andreas 82
Treppel, Leander 380
Triki, Abdelhamid 103
Troika 129
Trump, Donald 242, 375, 385
trust 197, 204
Tsipras, Alexis 148, 151
Tunisia
  applications for EBRD funding 103–4
  first projects 109
  GDP growth 121*t*
  included in SEMED 104
  investment in 113–14, 122*t*
  protests 91
  regional offices 112, 119
  suicide of street vendor 91–2
Turk Ekonomi Bankasi (TEB) 261
Turkey
  Ankara Agreement (1963) 9
  application to be country of operations 30–6

banking sector 258–61
bonds 295
Borsa Istanbul 296
as choice for potential expansion 13–14
companies involved in EBRD financing 13
controversial decision to invest in 7–8, 20–5
as country of operations 35–43, 85
and Cyprus 10, 17–18
EBRD management dilemma over 11–24
EBRD management response to 25–30
EBRD shareholders views 20–5, 31
economic arguments 29–30
economic growth 15
energy intensity 427
and EU accession 27, 30, 36, 38, 42
and the European Union 8–10
GDP growth 15, 124, 424
Gender Action Plan (GAP) 254–5
interest in EBRD 14–20, 37–8
investment in 41–3, 167, 184–7
as largest country of operations 39–43, 167
legal arguments 25–9
and Paris Agreement 377
per capita income 421, 422*f*
political arguments 29
private sector 40, 43
reflections on becoming a country of operations 36–9
role of women 40–1
SEFFs 369
state control and intervention 27
Strategic Review on formal application 33–6
sustainable energy projects 41, 43
and Syrian refugees 265
and transition purpose of EBRD 25–6
Turkish Lira Overnight Reference Rate (TLREF) 299
views on as recipient country 23–4, 31
women in 254–5
Women in Business programme 258–61
TurnAround Management (TAM) 245
Turnbull, Jim 291
TurSEFF 369
2030 Agenda for Sustainable Development 227, 263
Tymoshenko, Yulia 168, 172, 174–5

U

Ukraine
after Revolution of Dignity 184–93
annexation of Crimea 165, 175
anti-corruption efforts 184, 186–7, 188–9, 192–3
banking sector 191–3
building project 188
Business Ombudsman Institution (BOI) 192, 311–14
conflict 165, 174, 187
corporate governance 331–4
corruption 168–72, 175, 184, 185–6, 307, 320–1
derivatives 293
EBRD operating in again 184–93
energy sector 188–91
financial support 66
gas sector 188–91, 331–4
'gas wars' 172–3
GDP growth 179
Gender Action Plan (GAP) 253, 254
good governance 319
and halt to finance in Russia 179–80
and ICGI 306, 307, 311
Integrated Approach (IA) 212
investment in 184, 187
KievPrime 279
and Legal Transition Programme (LTP) 319
Maidan Revolution 174–5
Minsk Protocol 187
nationalisation 191–2
and NATO 159
protests 174–5
public procurement 319–22
ranking in UN e-participation index 321–2
reforms 187–92
regional offices 187
and Russia 164–7, 168, 172–3
supporting reform and investment in 184–7
suspension of EU talks 172–4
transport infrastructure financing 186
UONIA 299
war in 187
Yanukovyich era 167–9
Ukraine National Reforms Council 187

Ukraine Reform Architecture (URA) project 188
Ukrtransgaz (UTG) 189, 332
Ulyukayev, Alexei 178, 182
unemployment 116, 127, 250
UniCredit 69
Union for the Mediterranean (UfM) 88
Union of Soviet Socialist Republics (USSR) 29
United Bulgarian Bank 344
United Kingdom (UK)
  and extension of remit 100
  Good Government Fund 309
  view on transitory nature of EBRD 22
  view on Turkey as recipient country 7, 23–4, 31, 34
United Nations (UN)
  e-participation index 321–2
  Framework Convention on Climate Change (UNFCCC) 337
  and Georgian conflict 161
  Legislative Guide on Insolvency Law 323
  Summit on Sustainable Development 370
  Sustainable Development Goals (SDGs) 227
  Third International Conference on Financing for Development 227
Urengoy-Pomary-Uzhgorod pipeline 189
USA
  and extension of remit 98–9
  and Greece as country of operations 147
  relationship with Russia 22–3
  as shareholders 418–19
  and tensions between Russia and Ukraine 165
  view on transitory nature of EBRD 21–2
  view on Turkey as recipient country 7, 21–3, 31, 33, 34–5, 37
Uzbekistan 28, 170, 310

V

Vakifbank 261
van Nederveen, Axel 297–8
Varoufakis, Yanis 148
Vattenfall Institute of Economic Research 355
Vekselberg, Viktor 326
Vice Presidents 217
Vienna Initiative 58, 66–71, 79–82, 272, 285–6, 324
Vienna Initiative 2.0 80–2
Vienna Initiative Working Group on Local Currency and Capital Markets Development 285–6
Vienna Plus 79–82, 285–6
Vital Infrastructure Support Programme (VISP) 399–400
Vlaanderen, Paul 232
von der Leyen, Ursula 434
Vujčić, Boris 69

W

water resources 370–1
West Bank and Gaza 104–5, 115–16, 121*t*, 122*t*
Wieser, Thomas 67
women *see also* gender issues 116, 243–4, 247, 249, 250, 260, 263
Women in Business (WiB) programme 41, 114, 245, 248, 258–62
Wood and Company 296
World Bank
  Doing Business index 30, 171
  and Georgian conflict 161
  policy dialogue 225
  Principles for Effective Insolvency and Creditor/Debtor Regimes 323
World Trade Organization (WTO), Agreement on Government Procurement (GPA) 320

Y

Yakovenko, Alexander 178
Yanukovych, Viktor 167–9, 172–5, 184, 185, 307
Yapi Kredi Bank 255
Yatsenyuk, Arseniy 186, 190–1
Yushchenko, Viktor 167, 174

Z

Zagreb Holding 295
Zanawi, Meles 365
Zettelmeyer, Jeromin 56–8, 82, 218, 252, 255
Zhamishev, Bolat 51
Zoellick, Robert 73
Zulfikar, Mona 392

The second volume of the history of the European Bank for Reconstruction and Development (EBRD) takes up the story of how the Bank has become an indispensable part of the international financial architecture. It tracks the rollercoaster ride during this period, including the Bank's crucial coordinating role in response to global and regional crises, the calls for its presence as an investor in Turkey, the Middle East and North Africa and later Greece and Cyprus, as well as the consequences of conflicts within its original region. It shows how in the face of the growing threat of global warming the EBRD, working mainly with the private sector, developed a sustainable energy business model to tackle climate change.

Transforming Markets also examines how the EBRD broadened its investment criteria, arguing that transition towards sustainable economies requires market qualities that are not only competitive and integrated but which are also resilient, well-governed, green and more inclusive. This approach is aligned with the 2015 Paris Agreement and the international community's 2030 Agenda for Sustainable Development, with its core set of 17 sustainable development goals. The story of the EBRD's own transition and rich history provides a route map for building the sustainable markets necessary for future growth and prosperity.

ABOUT THE AUTHORS

Andrew Kilpatrick is a consultant, providing advice to the EBRD, ADB and World Bank Group. Until 2018, he was executive counsellor to the Chief Economist at the EBRD and Director for Project and Sector Assessment in the Economics and Policy Group. He served on many of the Bank's key committees during ten years at the EBRD, and was responsible for providing advice to the EBRD's Operations Committee and Board of Directors relating to the transition of the Bank's countries of operations towards sustainable market economies. Prior to joining the EBRD, Andrew was a senior official at the UK's HM Treasury. In that capacity he held several positions, including heading the Group charged with tackling Financial Crime, Head of Global Economics, Head of Fiscal and Macroeconomic Policy and Deputy Press Secretary to the Chancellor of the Exchequer.
Andrew is the author of *After the Berlin Wall, A History of the EBRD, Volume 1.* and of a number of academic publications and was an Advisory Board member of the Centre for Business Research at the Judge Business School. A former research fellow of Sidney Sussex College, Cambridge and research scholar of Trinity College, Cambridge, Andrew holds degrees in economics from Cambridge University.

Anthony Williams is an experienced journalist and senior communications expert. Until 2020, he was Director of External Communications at the EBRD, having joined the development bank in 2006 as Head of Media Relations. He worked on communications for many key developments at the EBRD, including its response to the Global Financial Crisis, its expansion into new regions as well as its increasing focus on combatting climate change. Prior to joining the EBRD, Anthony spent a career spanning nearly three decades at Reuters News Agency. He was a foreign correspondent in Germany, France and Switzerland. He was West German Economics Editor at the time of the fall of the Berlin Wall. Between 1995–2006, he held various senior editorial positions, including Reuters Editor for the UK and Ireland; News Editor for Europe, Middle East and Africa; and Global News Editor.

ISBN 978-963-386-412-8

Central European University Press
Budapest – Vienna – New York
Sales and information: *ceupress@press.ceu.edu*
Website: *http://www.ceupress.com*