Counter
Balance
Challenging the European Investment Bank

Counter Balance
Rue d'Edimbourg 26
1050 Brussels
Belgium

T: +32(0)2 893 08 61
T: +32(0)2 893 10 35
Email :info@counterbalance-eib.org
counterbalance-eib.org

Counter Balance statement on the Commission's Impact Assessment of the External Lending Mandate of the EIB

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The aim of this written position is to contribute to the Impact Assessment (IA) led by the European Commission (EC). Therefore, Counter Balance and its member groups have identified the most crucial issues to be carefully examined by the EC through the IA procedure. The recommendations presented in this document have been designed in order to be used as concrete options for the future External Lending Mandate proposal covering the period 2014-2020.

The current External Lending Mandate of the European Investment Bank (EIB) contains several improvements compared to the previous version and includes various points that were raised by NGOs in the past. However, it leaves many concrete aspects to further decisions and allows a broad interpretation of important obligations. And above all, it increases the role and mandate of the EIB despite the Bank's poor record in terms of development impact, and in contrary to the conclusions of the external lending mandate review.

Therefore we urge the European Commission to press further in tying EIB lending as concretely as possible to legally enforceable criteria for the next funding period. We also have major concern about many of the sectors invoked to justify increased EIB lending, notably energy, climate change, microfinance and global loans, and ask the EC to secure major changes in the institutional culture and practice of the EIB before empowering it to extend its lending capacities.

Given the array of evidence that the EIB is not yet suited for a development role, we strongly oppose the possibility that EIB increases its overall investments outside the EU, extends the range of financial instruments offered, and undertakes concessional lending by mixing EIB money with EU grants.

European Union governments must resource and empower other institutions than the EIB to make progress on poverty reduction and environmental goals. There is a need to reshape the overall EU development finance architecture. This approach is in line with the key priority of the aid effectiveness agenda to reduce fragmentation and duplication among institutions. As it currently operates, we suggest that the scope and extent of EIB lending operations outside the EU with the Community guarantee be progressively reduced and become more selective according to few and clear priorities, until such time as the Bank can demonstrate consistent fulfilment of its development obligations.

I. Coherence of the ELM with EU development objectives and external action priorities

Coherence of the ELM with EU development objectives

The EIB ELM should focus on ensuring the achievement of the objectives set out in the Article 21 of the Lisbon treaty, support the cross-cutting EU development and human rights objectives and ensure positive development impacts on the ground. The EIB lending outside the Union should be made fully consistent with EU Development assistance framework and based on the implementation of key aid effectiveness priorities, including the recipient country ownership, alignment to recipient country developing strategies, as well as transparency requirements.

In order to apply the above mentioned principles, EIB should ensure a greater alignment with host countries national development plans and/or EC country strategies. The EIB should follow the EC strategic programming documents objectives, priorities and expected results while planning investments in specific countries. As it appears that EIB would greatly focus in 2014-2020 on the neighborhood region, it is important to ensure that EIB, along the Union and its member states, „*should ensure the coherence and the complementarity of their respective policies on cooperation with neighboring countries*“, through participation in the joint programming exercise and formation of the Single Support Framework (as proposed by the EC in the European Neighborhood Instrument 2014-2020), and its implementation.

On operational level and in order to achieve the EU development cooperation objectives, it seems crucial that development outcomes are the overriding criteria for project selection and evaluation, including by developing clear outcome indicators, and complying with highly responsible investment standards (see Part V of this document).

Regional Operational Technical Guidelines

The aim of developing Regional Operational Technical Guidelines is to strengthen the consistency of EIB external actions with the external policy objectives of the EU, therefore it should be an essential element of the new mandate. In addition, it is important to set the procedure and timeframe for regular updates and review of operational guidelines on a bi-annual basis, and in line with EU priorities (as defined by the EP and EEAS) within the regions. Civil society organizations in the beneficiary countries should also regularly be involved in a consultation process to provide feedback on priorities definitions. This is even more crucial as in neighborhood region the principle of "More for More" and subsequently the "Less for less" principle will be introduced. Therefore through the regional guidelines the EIB should be able to follow all policy changes identified by the Union and engage the countries towards more integration.

Blending

Another area of concern is the use of innovative financial instruments, and especially the blending of loans and grants. At the time being, such a blending would happen without clear development criteria detailing positive development outcomes expected. Indeed, if the EU aid is blended with loans and other forms of financial investments, it should be ensured that the EIB's operation do not only support poverty reduction, respect the political, socio-economic and cultural rights of the people but also ensure the same level of transparency and accountability as official aid, while not adding further debt burden to host countries.

So far the EIB blending operation has not sufficiently demonstrated the development impact of blended finance. On the contrary, blending tends to rather support development of large scale investment projects with great potential to undermine the socio-ecological rights of affected people, while being questionable from a development and financial additionality point of view.

In its report, the Wise Persons Panel that reviewed the EIB's ELM recognized that EU needs to do more to ensure that its external assistance is in line with the aid effectiveness agenda. It stressed that "*In the developing countries, the importance of aid effectiveness will become even higher, and the EU will be expected to lead actions to improve the delivery of financial assistance in the interest of the beneficiary countries and of EU policy objectives. Despite numerous achievements, the European external assistance remains too fragmented and not yet fully in line with the European Consensus on Development and with Aid Effectiveness agenda*".
Despite the fact that a Group of Experts (GoE) has been set up and some work has been undertaken we consider that there is still a limited evidence base for promoting blending in the framework of the establishment of a Platform for Cooperation and Development as proposed by the GoE**.**

Recommendations*:*

- The EIB should not be equipped with a concessional finance window blending loans and grants and thus performing concessional lending. A clear management line for the EIB external lending, different from the one dealing with the lending in the EU, should be set up within the Bank.
- The accountability and transparency of blending mechanisms should be properly addressed in the next EC proposal on the ELM. Meanwhile, there should be a clear demonstration of the added value of the grant element, and the EIB should be required to report on the additionality of this blending.
- It would be in the interest of the EIB to engage, before the establishment of the platform, in a comprehensive review and evaluation of existing facilities, based on its recently developed Results Measurement Framework (REM) to be implemented throughout 2012. On the basis of the results of this review, and in deep cooperation with all relevant stakeholders including final beneficiaries, the EIB should consider how it will align new blending mechanisms with aid effectiveness principles and comply with the objectives of the European Consensus on Development.
- By increasing its loan-based development finance through blending, EU development finance contributes to the further indebtedness of developing countries. This element has not been sufficiently taken into account when assessing the impacts of blending.

II. Energy and Climate Change action

We are welcoming EIB's portfolio shift in favour of renewable energy sources in recent years. However, serious concerns with regards to EIB's overall energy portfolio remain: the potential of energy efficiency remains largely unutilised, lending to fossil fuels (including coal) still keeps increasing as well and regional imbalances in renewable energy lending remain huge. Outside of the EU the EIB still lends twice as much to fossil fuels as to renewables and only 1% goes to energy efficiency. For a detailed outline we refer to Carbon Rising, a 2011 Bankwatch report[1].
We hope these concerns will be taken into account when the EIB will revise its energy policy and when it drafts the "strategy on how to gradually and steadily increase the percentage of projects promoting the reduction of CO2 emissions and phase out financing projects detrimental to the achievement of EU's climate objectives" as outlined in the revision of the previous ELM and required for the next ELM.

For an informed discussion around the new ELM we consider it as crucial to do an evaluation of the activities taken so far. Therefore, we have identified a set of questions on which we would like to be informed more into detail before fully engaging in the discussion:

[1] Bankwatch, 2011, Carbon Rising: http://bankwatch.org/sites/default/files/EIB-carbon-rising.pdf

- Where is the "strategy on how to gradually and steadily increase the percentage of projects promoting the reduction of CO2 emissions and phase out financing projects detrimental to the achievement of EU's climate objectives" at?
- Is this strategy and the definition of "projects detrimental to the achievement of EU's climate objectives" going to be discussed with interested parties before and published after finalisation? How will the strategy play into the next ELM?
- What are the criteria the EIB uses to define a climate project? Is there any need to prove a positive CO2 reduction including a long term perspective (Is there an assessment whether short term gains in efficiency lead to a longer term use of fossil fuels; or whether sequestration actually helps reducing CO2)?
- What kind of projects have been financed under the Climate Change Mandate? Will there be a discussion about what kind of projects are eligible under the Climate Change Mandate?
- How does the EIB assess these projects and CO2 reductions and how do they report about these projects?
- Will there be a consultation about the Climate Change Mandate in order to assess it before the next ELM is adopted?

Our concerns about over-reliance on carbon markets

Looking into EIB's actions on combating the climate crisis, these include a series of projects with highly questionable climate effects. The EIB has for example been active in establishing carbon funds, facilities and instruments to shore up EU's reliance on carbon markets as a solution against climate change. However, an increasing body of evidence shows that carbon trading does not help in reducing emissions and continues to allow business-as-usual pollution in Europe[2].

According to an analysis from 2011[3] the EIB manages six main carbon funds (partly together with other financial institutions) which have pledged EUR 589 million to purchase pre-2013 and post-2012 project carbon credits by financing offset-projects that reduce CO2 emissions through energy efficiency, renewable energy, avoidance of venting/flaring gas, fuel-switching from carbon intensive to less carbon intensive and sequestration of greenhouse gases through forestry.

Beyond these carbon funds the EIB is looking to invest in forest carbon and REDD (Reducing Emissions from Deforestation and Degradation) projects which are so far not yet included into compliance carbon markets. It would do it through investing in the Althelia Climate Fund and by issuing a first-of-its-kind 'rainforest bond'. These kinds of projects may result in land grabbing by privatising forests, industrial biofuels, monoculture tree plantations, GM crops and biochar projects. It is important to note that the bank acts here as a mere bank, developing new financial products rather than acting as the policy driven bank it presents itself.

The EIB's role in carbon finance, including its funds that spur on the EU ETS and carbon offset projects, allows EU Member States to avoid real cuts in emissions through legislative measures. After seven years, the EU ETS has clearly failed to incentivise internal emission reductions and investments in renewable and energy efficiency measures. Instead, the creation of a carbon commodity and related financial markets creates financial instability and volatility, which poses a major threat to fragile economies and impoverished communities. And the so far pursued solutions to climate change avoid the provision of appropriate, public finance for adaptation and mitigation

[2] By way of example we refer to 'Carbon Trading : how it works and why it is controversial' by Fern, 2010: http://www.fern.org/sites/fern.org/files/tradingcarbon_internet_FINAL.pdf
[3] Counter Balance, 2011, Banking on carbon markets: http://www.counterbalance-eib.org/wp-content/uploads/2012/07/Banking-on-carbon-markets_0.pdf

measures in developing countries.

Recommendations:

- Concerning mitigation actions, we see the main role of the EIB within the EU, which remains a major CO_2 emitter compared to neighbouring countries. It is here that EIB should help transforming industry and public infrastructure to curb emissions and build more democratic, sustainable and small-scale production systems as well as more democratic, effective and controllable distribution networks. It should use the review of its energy lending to develop a clear strategy that includes:
  - How to increase lending for energy efficiency within all member states and neighbouring countries, excluding investments that cause lock-ins into unsustainable energy infrastructure such coal plant lifetime extension;
  - How to increase lending for renewable energies taking into account strict environmental and social standards, excluding large dams and biofuels;
  - How to phase out support for fossil fuel projects;
  - A reassessment of the carbon footprint of EIB's entire portfolio in order to strategically change the interventions in the energy, transport and industrial sector; this would need to include the financial intermediaries.

  The next ELM should make reference to these strategies and integrate them into EIB priorities for lending outside the EU.

- Concerning funding for adaptation: the European Union should prioritize the financial support in developing countries for adaptation through the existing UN Adaptation Fund, and restate its support for the establishment of a Green Climate Fund under the UNFCCC on Climate Change, to be managed in a democratic and transparent way by institutions and agencies independent from IFIs and other financiers, such as the World Bank and the European Investment Bank.

- Regarding Carbon Funds, as a result of the dysfunctions and failure of the ETS, we ask for a moratorium on all carbon funds to be put in place.

- When lending outside the EU, the EIB should:
  - Finance only projects, whose underlying goal is poverty eradication and ensuring access to energy for the population of the relevant country,
  - Finance projects that contribute to increased democracy through enhancing public participation in its decision-making process,
  - Finance only those clients, who have committed to observe environmental and social standards which are not weaker than those in the EU. The integration of environmental considerations into the project appraisal process should be on the same level as in the EU, without exceptions,
  - Reconsider the relevance of its "major projects" approach (such as the Desertec project) and its regular recourse to lending to financial intermediaries including private equity funds,
  - Stop financing the interconnection system planned to scale up electricity production in neighbouring countries to serve the energy needs of Europe, as this is not the suited model for transforming the European energy system towards sustainability and decarbonisation,
  - Follow a path of energy coherence with the precautionary principle and development, environmental, democracy and human rights objectives of the EU, rather than serve only energy security objectives.

III. Changing the regional scope of the mandate

The new External Lending Mandate needs to further straighten horizontal high-level objectives for EIB financing operations across all eligible regions to respond to the global financial crisis and changing economic, social and environmental situation. In addition to the principles of the Union external policy (as defined in art. 21 of the TEU) the operations of the EIB globally should respond to the need of mobilization of limited public resources directed towards targeted, sustainable, inclusive and innovative investments as envisaged by the Europe 2020 Strategy.

Recommendations:

Following principles and practices should be applied to ensure added value of the EIB investments outside the EU:

- The EIB should refrain from investing in countries with corrupt, oppressive and totalitarian regimes. Functional democratic governments, free media and free right of association and demonstration are fundamental for ensuring effective and long term investments.
- The EIB needs to assess previous investments in the regions under the ELM, in order to identify their added value and contribution to the sustainable development of these regions and to Union's principles. In this regard, a particular attention should be given to the North African region where support to corrupted and authoritarian regimes largely took place in the past decades.
- Lending to the ALA regions should be stopped. Increased development support for low income countries of these regions should be prioritised in existing EU mechanisms (Development and Cooperation Instrument), IFIs and new regional institutions.
- Regarding lending to neighbouring regions (Eastern and Southern) the EIB should lead stringent development and human rights due diligence and adopt clear priorities in line with overall horizontal development and human rights objectives of the Union's external action. The effectiveness of EIB activities and its relationship with the ENPI instrument in EU neighbourhood should be reviewed once again before the issuance of a new external mandate in 2013.

IV. Financing private sector and SMEs through financial intermediaries

In order to reach small and medium sized enterprises the EIB has increasingly engaged in intermediated lending. This mechanism which requires financial intermediaries, mostly commercial banks, to on lend large so called 'global loans' in small portions to the ultimate beneficiaries comes with a number of challenges which may undermine a positive development impact. Intermediated loans come with reduced transparency and due diligence, the intermediaries are not necessarily development oriented and more than often operate through tax havens. To present these issues have not been addressed properly by the bank.

A main critique echoed on many occasions by civil society, the European parliament and academics is the lack of transparency inherent to this type of lending. Information about the ultimate beneficiaries is not made public due to commercial confidentiality clauses in the contract with the financial intermediaries. This makes it impossible to assess the economic and social impact of the loans and prevents a targeted approach to certain sectors or types of SMEs.

Additionally, by outsourcing part of its lending, the EIB outsources part of its responsibilities as well. Therefore the reliance on third parties for the carrying out of due diligence is a dangerous trend which can seriously undermine the quality and the positive outcome of the lending. The EIB should at all time remain responsible and provide more clarity on how these procedures are carried out in order to improve transparency and avoid misuse of funds.

A third problem lays in the nature of the financial intermediaries the EIB works with. They are mostly western commercial banks with little or no interest in development and often operational in tax havens. Since these intermediaries swallow part of the loan related benefits the EIB actively strengthens a western type of financial sector which is not adapted to the needs of local economies[4].

Actually, further effort is needed to ensure that EIB investments reach a broad range of beneficiaries. Recital 19 from the current ELM reads: "*In order to effectively reach out to SMEs, the EIB should cooperate with local financial intermediary institutions in the eligible countries, in particular to ensure that part of the financial benefits is passed on to their clients and provide added value compared to other sources of finance*".

Counter Balance is especially concerned about the use of a specific type of financial intermediary, namely private equity funds. These funds suffer from the same inadequacies as other intermediaries such as a lack of transparency and due diligence but its exclusive profit driven motive at the benefit of the investors rather than the beneficiaries makes its shortcomings even more explicit. Private equity funds seek high and short term returns at all cost. Moreover the so called 'hot money' involved may undermine long term financial stability.

The EIB has been a recent entrant in the microfinance sector, although growing steadily through the years. From traditional credit lines and loan guaranties, EIB's microfinance strategy has become particularly sophisticated and is now relying on financial intermediaries to allocate funds. There are growing concerns that only a small fraction of this money is actually reaching the hands of the poorest. A major obstacle is that the EIB embraces a wide definition of microfinance and lacks a clear vision. Insufficient portfolio monitoring is another element of concern of EIB's microfinance operations. The Bank produces very scarce information on the performance of these investments, and there is no concrete evidence that they are contributing to social progress in poor countries. In addition, increasingly microfinance is seen as a mean to expand and deepen the financial sector, rather than simply to provide credit to specific target groups. Social performance has been generally subordinated to the goal of financial sustainability, and this can help to explain why EIB's microfinance strategy is not always consistent with European development policies and their ultimate goal of poverty eradication.

More generally Counter Balance questions the effectiveness of EIB's private sector support. Claims that investments to the private sector don't go to where they are most needed and that they lack ownership – important to improve aid effectiveness – are confirmed by a Eurodad research[5] which found that 35% of the projects are owned by companies in OECD countries, only 25% are owned by a company in the countries where the project was based and 25% of the companies are based in tax havens.

Recommendations:

- The ELM should require granting Community guarantee only for financial intermediaries not operating in offshore financial centres, which have substantial local ownership and are equipped to implement a pro-development approach supporting the specificity of SMEs in each country.
- We advise the bank to exclusively work with locally embedded intermediaries that are focused on providing financial services to the poor in a responsible and transparent manner or supporting sustainable development more widely.

[4] Counter Balance, 2010, Hit and run development http://www.counterbalance-eib.org/wp-content/uploads/2011/01/Hit-run-development_WEB.pdf

[5] http://eurodad.org/wp-content/uploads/2012/05/Private_profit_report_web211.pdf

- The EIB should not use private equity funds as financial intermediaries given their focus on high returns contradicting a pro poor approach.
- The EIB should not extend its microfinance portfolio. Prior to a potential expansion, the Commission should require the EIB to define a clear microfinance strategy, assess its past microfinance activities outside the EU and introduce clear social performance based elements as well as transparency and accountability mechanisms.

V. Towards a result-oriented approach based on sustainable indicators and further accountability

Counter Balance is highly concerned by the lack of a result based approach in EIB activities outside the EU, as well as by the absence of an adequate framework for reporting on development and environment results.
Under the current ELM, the EIB is required to develop performance indicators to measure the development outcomes of its activities. Nevertheless, the development of the Results Measurement Framework (REM) - a newly created system of reporting that is supposed to be progressively implemented throughout 2012 – has not been yet entirely achieved. For instance, little information is available at the time on how this framework is used by the EIB, and the few examples disclosed on the website do not provide a genuine overview of the REM.

In addition, the Article 6.2 of the current ELM urges the EIB to develop a set of performance indicators in relation to development, environmental and human rights aspects of projects funded. Indicators being at the core of a result-based approach, they should be made available to the public as well as to the EC and the EP, and be subject to a public debate. Counter Balance calls for the EIB to ensure that sustainable development indicators are integrated into mainstream policy mechanisms, instead of being an environmental and social "add-on" to core statistical, measurement and reporting systems.
Such indicators should take into account "the relevant indicators under the Paris Declaration for Aid Effectiveness", as stated in the current mandate. The Paris Declaration commits its signatories, which include the EU, to take action to strengthen "*ownership", "alignment", "harmonization", "results" "and mutual accountability"*. It presents a monitoring framework to assess progress toward fulfilling these commitments, based on 12 actionable indicators, in particular indicator 9 on "*aid flows provided in the context of programme-based approaches"*, and indicator 7 on "*aid predictability*".
In order to fulfill the Paris Declaration's principles as required, the EIB should engage in a process of dialogue with beneficiaries of its operations in the Global South to ensure that its activities are aligned with beneficiaries (Global South governments) priorities and it fits in beneficiaries led process of development. This dialogue should be kept not only on the level of national governments, but also at regional or local level through inclusion of the civil society.

Regarding accountability and local ownership, not only the citizen's role, but also the role of national parliaments in decision making about project investments is often marginalized, since most of the time national parliaments are unable to get a foothold in project decision making[6]. Their involvement in the process would represent a better guarantee that investment decisions outside the EU do not breach the general principles of democracy and the rule of law.

In relation to Article 7 on Development related aspects, the EIB in the first place is accountable to people affected by financed projects, independent of origin and or location. As a target audience for its investment activity both the poor and affected people should be included. The project promoter is required to carry out consultations and disclose the results to the public. However, it is also crucial

[6] http://www.brettonwoodsproject.org/art-183338

to involve citizens already in the initial problem analysis and the planning and design stage of any project activity.

When disclosure is denied, the EIB has the burden of showing that the information requested falls within the scope of one or more exceptions. Exceptions in favor of non-disclosure should refer to a legitimate interest and incorporate a harm test, a bare reference to an exception being insufficient. Disagreements between requesters of information and the Bank should be subjected to an appeal process. The establishment of an enhanced and separate office under the auspices of the European Ombudsman for dealing with access to information regarding EIB activities outside the EU should be considered.

Recommendations:

- The new ELM should require the Results Measurement Framework to be reinforced and fully operational for the next funding period. Besides that, the EIB should report on it to the EC and EP.
- The EIB should report on the performance indicators it developed and make its findings public. In addition, the ELM should require that a set of sustainable development indicators are adopted following thorough consultation with beneficiary countries and local civil society organizations.
- The EC should ensure that the EIB will implement the requirements of the Paris Declaration for Aid Effectiveness, including the outcomes of the HLF on Aid Effectiveness in Busan.
- The Aarhus Convention and the ESPOO Convention with regard to transparency and accountability should be explicitly part of the next ELM.
- An accountability mechanism for the ELM should be developed for straightening the effectiveness and accessibility for the affected communities. Independence and shorter period of initial assessment of the complaint should be ensured tighter by increasing the capacity and responsibility of the EU ombudsman in terms of assessment.

Counter Balance coalition includes members from: Central and Eastern Europe: CEE Bankwatch Network; France: les Amis de la Terre; Germany: Urgewald; Italy: Re: Common; Netherlands: BothEnds; United Kingdom: Bretton Woods Project

Contact information:

Xavier SOL
Counter Balance coordinator
Rue d'Edimbourg 26, Brussels 1050
tel. + 32(0)2 893 08 61
fax. + 32(0)2 893 10 35
Email: xavier.sol@bankwatch.org
www.counterbalance-eib.org