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Challenges for the Council of Europe Development Bank (CEB)

Report[1]
Committee on Social Affairs, Health and Sustainable Development
Rapporteur: Mr Tuur ELZINGA, the Netherlands, Unified European Left

Summary

In these harsh economic times, alleviating social suffering is a major political priority – and duty – for Council of Europe member States. For this, many countries can count on the support of the Council of Europe Development Bank (CEB), a singular investor with a social vocation. The Bank as such has astutely steered through the bumpy economic environment and new regulatory constraints of recent years by adapting its orientations, structures and governance. It needs to persevere in the same direction, building on the shared sense of common purpose and ambition by its members.

The report encourages the Bank to keep strengthening its ties with the Council of Europe so as to maximise its impact and comparative advantage, notably in niche activities. Sectoral priorities (including the judiciary, public services, health-care, social housing and asylum facilities) and non-EU countries in South-East Europe require more fresh investment alongside projects to support employment. Parliamentarians, too, could play a more active role in domestically promoting project initiatives.

Further recommendations to the CEB insist on the need for continued improvements in governance and project quality. They feature proposals for reaching consensus on various reform options and a timetable, cooperation with institutional partners and member States on project development, efforts to boost direct financing of projects and the Bank's visibility, as well as action to strengthen impact evaluation of projects in the field of employment.

[1] Reference to Committee: Request for inclusion in the agenda of the session, Reference No. 3879 of 25 June 2012.

A. Draft resolution[2]

1. As the financial and economic crisis still haunts Europe, many countries are struggling to restore growth, employment and living standards to pre-crisis levels. With austerity measures and chronic underinvestment entrenched, social suffering has reached unprecedented levels. In these harsh times, multilateral development banks – such as the Council of Europe Development Bank (CEB or "the Bank" hereafter) – are key partners in sustaining public, social and economic investments, notably in areas where the private sector alone would not venture to go.

2. The extremely uncertain economic situation and new regulatory constraints have prompted the CEB to adapt, as necessary, its priorities, working methods, internal structures and governance in order to deliver "more with less". The Parliamentary Assembly welcomes the Bank's capital increase (effective from the end of 2011), efforts to expand the membership and to boost the social added value of projects, as well as steps to adjust internal structures and strategies. The implementation of the Development Plan for 2010-2014 and the adoption of a new Development Plan for 2014-2016 are crucial to the Bank's continued success.

3. The Assembly notes the Bank's continued commitment to preserving the level of lending to the neediest countries (notably those outside the European Union) without undermining its own risk profile, stable performance and profitability. The Assembly appreciates the fact that, despite the grim economic situation, no member State has failed to pay back loans, helped by the Bank's willingness to and assistance in redesigning some ongoing projects to help countries in budgetary difficulty. Although the demand for CEB loans temporarily decreased over 2011-2013, the interest in new projects is picking up again, with a strong emphasis on employment-support measures.

4. The Assembly believes that there is still much room for strengthening the CEB's ties with the Council of Europe, with a view to maximising its impact and its comparative advantage. Niche activities with high social value should be further expanded. They concern in particular sectoral priorities – like investment in administrative and judicial public services, small-scale health-care projects, social housing and asylum centres – and a geographical focus on non-EU countries in South-Eastern Europe.

5. Noting the Bank's increased emphasis on employment-related support and its intention to launch innovative financing for essential public services, the Assembly considers that the CEB could expand its participation in underpinning public-private undertakings for vocational training, skills development, professional counselling and job placement for young people. As appropriate, this support might usefully be extended to other vulnerable groups, such as persons with disabilities, minorities and displaced or migrant persons.

6. The Assembly stresses the importance of direct contacts between the Bank and the parliamentary representatives of European States for enhancing the visibility of the CEB's work and potential. National parliaments can play a most valuable role in promoting domestically project initiatives for the CEB's potential financing. The Assembly also invites the parliaments of Andorra, Armenia, Austria, Azerbaijan, Monaco, the Russian Federation, Ukraine and the United Kingdom to press their respective national governments to consider joining the CEB at the earliest opportunity.

7. In the light of the above considerations, the Assembly recommends that the Governing Board of the CEB:

7.1. with a view to continued rationalisation of the CEB's governance:

7.1.1. urge member States to enhance the coordination of national positions taken by their representatives on the Bank's collegial bodies (Administrative Council and Governing Board) and strive for reaching consensus within the Governing Board by actively looking for compromise solutions;

7.1.2. build a graduated approach to tackling pending governance issues by organising informal consultations among the members on various reform options and timetable;

7.1.3. in line with recommendations in the CEB Strategic Review of 2008, adjust statutory provisions or agree on their interpretation in a more flexible way so as to streamline decision-making structures;

[2] Draft resolution adopted unanimously by the Committee on 12 May 2014

7.1.4. simplify the voting system in the Governing Board, including for decisions on the appointment of top officials;

7.1.5. entrust the Governor of the Bank, seconded by Vice-Governors whenever necessary, to chair the meetings of the Administrative Council after the mandate of the latter's current Chair expires;

7.1.6. make the Governor of the Bank the CEB's external representative;

7.1.7. in addition to the Secretary General of the Council of Europe, associate closely and invite the Human Rights Commissioner and the President of the Parliamentary Assembly, as well as the parliamentary rapporteur on the CEB, to the annual meetings of the Governing Board and the joint meetings of the collegial bodies;

7.1.8. consider holding one of its meetings each year in Strasbourg;

7.2. in order to further increase project quality and the pertinence of project proposals emanating from member States, ask the CEB's Governor to ensure that the Bank:

7.2.1. strengthens its links with the Office of the Council of Europe Commissioner for Human Rights and systematically takes into account the findings of his country visits;

7.2.2. fully exploits complementarities and synergies with the European Investment Bank (EIB), the European Bank for Reconstruction and Development (EBRD) and, whenever appropriate, other international financial institutions;

7.2.3. assists member States concerned in building their capacity to absorb EU structural funds, in particular for developing projects in priority sectors such as the judiciary, small-scale health-care projects, social housing, asylum facilities, Roma integration and employment-related services for young people, people with disabilities, minorities and migrants;

7.2.4. enhances recourse to the combination of loans and grants for the support of projects with the highest social-impact potential;

7.2.5. strengthens the monitoring and evaluation of the impact of the projects financed in the field of employment in terms of real and sustainable job creation or preservation in the countries concerned;

7.2.6. in line with the strategic objectives of its Development Plan for 2014-2016, enhances the direct financing of projects, in particular in favour of public bodies;

7.2.7. supports member States' loan projects aimed at implementing the recommendations set out in the 2014 report by the Council of Europe Secretary General on the "State of democracy, human rights and the rule of law", notably as regards social rights and the Disability Action Plan 2006-2015;

7.2.8. perseveres in boosting its visibility both among non-member countries and those member States that are not active borrowers.

8. The Assembly looks forward to receiving the [written] replies of the Governing Board and the Governor of the CEB to the above recommendations.

B. Explanatory memorandum by Mr Elzinga, rapporteur

1. Introduction: the CEB mission and ties with the Council of Europe

1. Over the last years and since the latest report of the Parliamentary Assembly on the Council of Europe Development Bank (hereafter "CEB" or "the Bank") in 2010, the socio-economic landscape in Europe has been radically transformed by the financial and economic crisis. Many countries are struggling to restore growth and living standards, while social hardship has sprawled across society. In these difficult times, multilateral development banks are important actors in supporting solidarity between and within countries and stepping in where the private sector alone would not venture to go.

2. The CEB plays a special role in alleviating the social crisis sparked by the economic crisis and austerity measures, since it has a unique social vocation. At the same time, the external constraints and changing economic circumstances are challenging development institutions to work differently and to deliver "more with less". The Council of Europe Development Bank is perhaps even more challenged than its peer institutions in Europe, since in 2012 two of the three rating agencies downgraded the Bank from AAA to AA+, as a consequence of the downgrading of many CEB member countries and borrowers.

3. The Bank is a partial agreement of the Council of Europe that currently groups 40 States[3] (eight member States[4] have opted not to take part in this agreement so far) and which Kosovo*[5] joined on 4 November 2013. The Parliamentary Assembly has been following the Bank's work more closely since the early 1990s when the CEB underwent important structural transformations and rapidly integrated many new members from central and eastern Europe.[6] More recently, both the Council of Europe and the Bank have tried to reform their functioning, so as to become more relevant, focused and efficient in accomplishing their respective missions.

4. The Bank's member countries can use the CEB as an instrument, but also a partner, for supporting social projects. They have a direct interest in that this institution has sufficient means and clear objectives to pursue its social vocation. Its relation with the Council of Europe and its commitment to the Council of Europe's political and social objectives are of crucial importance for the Bank's existence and purpose. The impulse from the Committee of Ministers' representatives, who sit on the Bank's Governing Board to provide a strategic orientation, is therefore essential for the CEB to succeed. Just as crucial is the close cooperation between the Bank and other Council of Europe entities. In this respect, the Parliamentary Assembly seeks to contribute proposals for optimising the Bank's work and to facilitate discussions regarding its future.

5. This report will review the CEB's activities in recent years (2010-2013), follow up on the Assembly's earlier recommendations and assess progress in the Bank's strategies to adapt to changes in its environment and on the Bank's internal strengthening. I am grateful for the information and insights I was able to obtain in particular from the relevant documents[7] of the Bank's main working structures and meetings with the various representatives of the Bank (Chairperson and selected members of the Governing Board, the Chairperson of the Administrative Council, the Governor, Vice-Governors and several directors), the Secretariat of the Partial Agreement on the CEB and some other officials. As the Assembly's rapporteur, I also attended the Bank's Annual Joint Meeting held on 14-15 June 2013 in Malta and the meeting of the Governing Board on 22 November 2013 in Paris.

2. Overview of the Bank's work in 2010-2013 in the light of Europe's economic woes: new dynamics in lending, risk management and cooperation with partners

6. Since the onset of financial crisis in Europe over 2008-2009, the CEB has seen economic turbulence spread deep and wide across its member countries. If in the beginning the financial storm caused a "credit

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[3] Albania, Belgium, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Georgia, Germany, Greece, Holy See (an observer State of the Council of Europe), Hungary, Iceland, Ireland, Italy, Latvia, Liechtenstein, Lithuania, Luxembourg, Malta, Republic of Moldova, Montenegro, Netherlands, Norway, Poland, Portugal, Romania, San Marino, Serbia, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, "the former Yugoslav Republic of Macedonia" and Turkey.

[4] Andorra, Armenia, Austria, Azerbaijan, Monaco, the Russian Federation, Ukraine and the United Kingdom.

[5] *All references to Kosovo, whether to the territory, institutions or population, in this text shall be understood in full compliance with United Nations Security Council Resolution 1244 and without prejudice to the status of Kosovo.

[6] Originally set up, in 1956, as a fund, this institution first focused nearly exclusively on the aid for the resettlement of refugees and displaced persons, as well as dealing with various emergency situations. Later, the expansion to the East brought a new focus on vast development needs in the new member States.

[7] This includes agendas, minutes, decisions and working documents of (the meetings of) the Administrative Council and the Governing Board and various communications by the Governor.

crunch" mainly for countries in central and eastern Europe, the situation rapidly deteriorated also in the West. Large shareholding countries that were at the heart of the Bank's high creditworthiness-and-risk profile have been downgraded several times, which inevitably led to the lowering of the CEB's own rating despite stable performance and profitability (see Table 1 in the appendix).

7. The CEB, as well as other multilateral development banks, came under increased pressure from international rating agencies which no longer consider callable bank capital as being of the same quality as paid-in capital. At the same time, regulators have been slow in recognising the special role multilateral development banks play and the need for specific provisions in regulatory frameworks in this respect. Incidentally, as from 2012, several major development banks (European Investment Bank, European Bank for Reconstruction and Development, World Bank and the CEB itself) changed their top leadership.

8. In addition to international investors getting wary of engaging across more and more European countries, the main rating agencies have tightened up the requirements on capital and leverage for financial institutions under their scrutiny. Fortunately, the Bank's capital increase became effective in the end of 2011: its funds thus grew from €5 to 6.5 billion.[8] This was an extremely timely and necessary step in order to meet tighter prudential standards and to preserve the level of lending activities, in particular in favour of countries where uncertainties and risks are greater.

9. A total of € 2.26 billion in loans was approved in 2010, €2.1 billion in 2011, €1.8 billion in 2012, and €2.27 billion in 2013. Funds disbursed were €1.78 billion in 2010, €1.85 billion in 2011, €1.58 billion in 2012, and €1.84 billion in 2013. Figures for 2013 are mostly a consequence of diversification efforts and of member States' increased interest in job creation and preservation. On average, CEB disbursements increased by 9% in the 2010-2013 period compared with the previous Development Plan period (2005-2009). We see a sort of convergence between the financing commitments for projects approved and those actually financed on the basis of earlier multi-year commitments. Given the delicate external environment, the last few years have represented a big challenge for the Bank.

10. The number of projects approved during the period 2010-2013 was 30 in 2010, 34 in 2011, 28 in 2012, and 38 in 2013. On average, two-thirds of projects approved were in favour of the neediest – target group – countries.[9] This group of 21 countries (22 including Kosovo from November 2013) consists of non-EU and new EU member States, roughly accounting for a half of CEB's members. Some of those countries have been progressing in terms of development much faster than others, which made it necessary to make clear distinctions between the better-off and the more disadvantaged countries for achieving greater added value through the Bank's projects.

11. In 2013, out of 38 projects approved, 27 projects (representing almost 50% of total amount of loans approved) were meant to benefit target countries. These figures show a continuous effort deployed in favour of the target countries and a balancing act of combining both the volume of activity and risk exposure. Overall, as indicated in Table 3 of the appendix, countries such as Croatia, Poland, Romania, Serbia, Slovakia and Turkey were the key beneficiaries among the target countries over the 2010-2013 period, whilst Belgium, France and Spain were the grand western recipients of the Bank's funds in the same period.

12. Concerning the number of countries actively borrowing from the CEB, this stood at 18 in 2010, 16 in 2011, 14 in 2012, a decrease mostly due to domestic budgetary constraints, and 22 in 2013. Some countries discontinued projects already on track: 13 projects (€ 242 million) were stopped in 2010, 20 projects (€ 140 million) in 2011, 15 projects (€ 540 million) in 2012, and 18 projects (€ 668 million) in 2013. However, there have been no non-performing loans. Thanks to the redesigning of some ongoing projects (such as those in favour of Cyprus) and better targeting of new ones, project activity picked up throughout 2013, with loan approvals rising about 27% and disbursements up by 17%.

13. In terms of sectoral distribution (see Table 2 in the appendix), activities mainly focused on fostering social cohesion, in particular job creation, urban and rural modernisation and social housing. The share of projects in this field grew from about 50% in 2010 to 79% in 2012 and 75% in 2013, while that in favour of environment-related work shrank, mainly due to budgetary constraints and use by the countries concerned of the EU funds (grants) instead of CEB loans. Support for public infrastructure with a social vocation remains an important area of activity, although the intensity of involvement in underpinning administrative and judicial

[8] The CEB's subscribed capital increased by about 50% from € 3.3 to 5 billion and the paid-in capital rose from € 370 to 554 million.

[9] Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Cyprus, Czech Republic, Estonia, Georgia, Hungary, Latvia, Lithuania, Malta, Republic of Moldova, Montenegro, Poland, Romania, Serbia, Slovak Republic, Slovenia, "the former Yugoslav Republic of Macedonia" and Turkey.

public services diminished considerably from 2010 to 2013 for the same budgetary reasons. I hope that this trend will be reversed because investment in infrastructure and training services in this domain is most valuable for the Council of Europe member States in strengthening the rule of law, not least under the Human Rights Trust Fund managed by the CEB.

14. In the light of profound social and demographic changes across Europe, the CEB's work in synergy with international, regional and local partners is of utmost importance. The Bank is particularly proud of developing its operations under the so-called Sarajevo process which implements the Regional Housing Programme in the Western Balkans (covering Bosnia and Herzegovina, Croatia, Montenegro and Serbia). This initiative enjoys the strong political and financial backing of the international community (the European Commission, the UNHCR, the OSCE and the United States). According to plans, the framework with € 600 million earmarked should benefit nearly 74,000 people (or some 27,000 households), especially refugees and internally displaced persons. Yet a number of European donor countries are dragging their feet on their pledges.

15. In a similar manner, the Bank is working with institutional partners to help the integration of Roma communities (some 12 million people are concerned in Europe). The latter suffer from sky-high unemployment rates, an insufficient level of education and healthcare, as well as from a poor housing situation. The Bank therefore follows the Council of Europe expert advice and participates in the Alliance of Cities and Regions for Roma Inclusion. In 2013, the Governor also met with the Special Representative of the Secretary General for Roma issues at the Council of Europe, and Bank staff regularly attends meetings and conferences on Roma issues. Priority projects are financed through a mix of loans and grants, with substantial co-funding from the European Commission, the World Bank and the UN agencies[10], and the contribution of various specialised non-governmental organisations.

16. As the recession was biting into European labour markets, the CEB boosted its support for job creation and preservation in micro-, small and medium-sized enterprises. This orientation accounted for nearly half of projects in 2012-2013 and about a third over the last five years, mostly in target countries.[11] Projects are essentially financed through credit lines to local banks and leasing institutions. Indeed, one in ten persons, or about 28 million people, are unemployed in countries covered by the CEB, and youth unemployment is hitting record heights in comparison with the rest of the population, notably in South Europe. Emphasis on skills development, professional counselling and mobility in the youth group, but also, as appropriate, among the disabled, minorities and displaced persons, is therefore particularly necessary.

17. Decent housing for low income persons and for the population in disadvantaged areas is a vital aspect of the CEB's mission to enhance social cohesion and to improve living conditions. Large multi-annual programmes of CEB investment have been put in place in Belgium and France to help poor first-time buyers of accommodation, renovation and improvements in energy efficiency of housing, as well as adaptation of dwellings to the needs of the elderly and the disabled. Such programmes could be replicated across all member States, because needs in this area are particularly acute; however, governmental partners of the Bank have to find ways of departing from austerity in favour of more social investment first.

3. Developments in strategy

18. Aiming to improve the Bank's performance and governance so as to meet growing expectations, member States carried out the Strategic Review of the CEB and its recommendations were submitted in October 2008. In 2011, the Chairman of the Governing Board launched a consultative process to explore possibilities for the implementation of these recommendations regarding CEB's governance structure (e.g. voting procedures).

19. Moreover, the Bank's new Governor, Rolf Wenzel, presented ideas for the longer term vision. Immediately after taking office, he launched a broad-based discussion on internal and external challenges for the CEB, including consultations with the Governing Board and the Administrative Council who welcomed and supported the initiative. This discussion yielded important improvements which have sharpened the social focus of the Bank (e.g. two pronged approach, reform of the social dividend account) and making CEB's work more efficient and transparent (e.g. job classification exercise and new prudential framework). In addition, responding to the changed financial and economic landscape in Europe and in particular in many of its member countries, the Governor launched, early in 2013, a review of the Development Plan with a view

[10] Notably the UN Development Programme (UNDP), the UN High Commissioner for Refugees (UNHCR) and UNICEF, UN Children's Fund.
[11] In November 2013, support for MSMEs (micro-, small and medium sized enterprises) became a separate line of action with the adoption of revised "Loan and project financing policy".

to clarifying the orientations of the Bank and strengthening its toolkit. The new Development Plan 2014-2016 was thoroughly discussed by the Organs of the Bank and approved by the Governing Board in November 2013. We shall look at these strategic areas one by one.

3.1. Implementing the recommendations of the Strategic Review

20. The CEB Strategic Review of 2008 proposed a series of steps concerning the Bank's mandate, relations with the Council of Europe, the financial and operational framework, relations with external partners (such as financial institutions and international organisations) and, perhaps most importantly, governance. In its Recommendation 1937 (2010), the Assembly strongly supported this process, notably on the proposed increase in the Bank's capital and improvements in governance. The latter concerned in particular the duration of the term of office of appointed officials, duties and responsibilities of Vice-Governors, simplification of the voting system in the Bank's organs, reporting of the evaluation mechanisms inside the Bank.

21. After lengthy and tedious discussions in the CEB's Governing Board and Administrative Council, some progress was finally achieved. As referred to in the previous chapter, the Bank's capital was increased. The selection and appointment procedure of the post of Vice-Governors has been modified to ensure the required professionalism and to balance managerial efficiency and the inter-governmental nature of the Bank. Concerning the evaluation functions, a relevant Bank's department has been renamed and ensures the participation of evaluators from the early stages of assessment of new applications for loans. Evaluators' reporting to the Governor and the Bank's organs has been aligned with international best practices (e.g. loan documents now include a dedicated chapter on "lessons learned" from evaluation). Moreover, the term of office of newly appointed officials (Governor and Vice-Governors) is now limited to two mandates maximum.

22. However, the consultations on adjustment to the voting system have not yielded results so far. This mainly concerns proposals supported by a number of smaller and medium-sized countries which sought to revise statutory requirements for majorities to be achieved in voting, such as for electing chairs of the Bank's organs or making important decisions on capital. The deadlock also continues in the Governing Board on the streamlining of the Bank's governance model. Despite these difficulties, member States have shown unity in adopting the CEB's new development plan.

3.2. Development Plans for 2010-2014 / 2014-2016 and the Governor's proposals for Reform

23. When its Development Plan for 2010-2014 was put in place, the Bank was confident that Europe was slowly recovering, although high unemployment and social needs were expected to persist. Three long-term trends of population aging, higher energy prices and larger financial needs of local authorities have continued to affect all member States. Against this background, the Bank was asked to provide further enhanced support to "priority" countries (that is, target group countries). The share of loans to these countries reached 61% of the total loans outstanding at the end of 2012, but the annual lending volumes dipped, largely because of lower demand from member States. Similar banks, such as the EIB, faced the same problem.

24. With the continued deterioration of the economic situation, the CEB was compelled to review its quantitative targets and pay greater attention to the balancing of risks in its portfolio. A review of the *Banque de France* of CEB's prudential framework and internal control system also called for adjustments in that direction.

25. The backdrop for discussions on the Bank's new development plan for the next three years was a clear understanding that major changes in strategy were needed. This was so because some of the earlier assumptions were no longer valid, earlier policy objectives were not all appropriate and former targets were no longer realistic. National governments are now concentrating on macroeconomic restructuring, debt refinancing and efficiency "savings" to the detriment of fresh investments. Even absorption capacity of structural and cohesion funds in EU countries diminished (54% on average, but as low as 26% in Romania and about 40% in Bulgaria, Italy and Malta). Pro-employment projects will remain of utmost importance for the Bank's relevance.

26. The CEB's Development Plan for the next three years emphasises the following strategic orientations:

- increased added value of loans and projects in favour of social investment;
- support to member States concerned in the absorption of EU funds, notably for the social sector;
- enhanced flexibility of loans and more 'client-needs-oriented' financing;
- greater support for jobs creation and preservation, in particular SMEs and start-ups;

- developing new ways of financing for strengthening social cohesion.

27. To ensure more added value, the Bank will provide additional technical assistance and project monitoring for countries with a high country index (in line with the two-pronged approach) by using grants. It might also participate in a project's financing above the current limit of 50% and support up to 90% of projects with the highest expected social impact. Whenever EU co-financing is envisaged, the CEB could pay special attention to the needs of accession countries or those covered by neighbourhood policies (7 CEB member States concerned).

28. The Development Plan for 2014-2016 is underpinned by the reform proposals that the Governor launched when he took office in December 2011. Under the heading "Addressing challenges" he introduced:

- a two-pronged approach was developed and started to be implemented in 2013 to improve the screening of projects in terms of potential social added value. This new method enables the Bank to weigh the merits of each new project on the basis of country rankings[12] and more in-depth project rating for the inherent social content. Systematically, for all the projects financed by the Bank, the method takes into consideration, among others, the sectoral context, the social impact as well as the institutional arrangements and the sustainability, with emphasis on the delivery of expected social and economic outcomes;
- a strengthened evaluation function in the Bank;
- increased transparency and explanation of loan documents;
- the reform of the Social Dividend Account (formerly "Selective Trust Account") from March 2013 allows the Bank to diversify its use of grants and to take valuable project-related side initiatives.

29. An important step will be attempts to launch innovative financing (programme loans) to under-funded public bodies that are crucial for maintaining viable public services. This means resources not only for investment, but also – on an exceptional basis – for operational expenditure to cover any existing or anticipated gaps. Such action will support sustainability of structural reforms and continuity of larger projects in a difficult economic setting. Moreover, it is foreseen to develop cooperation with the private sector (such as through public-private partnerships) and risk sharing mechanisms (mainly in favour of microcredit and improved access to finance for the vulnerable population).

30. In financial terms, focus on the target countries will be maintained. Actually, in terms of geographic distribution, the CEB aims at maintaining the 60/40 ratio of disbursements between the target and non-target group countries, on condition that the Bank preserves its financial soundness. Loan approvals are expected to recover to the level of 2010-2011 (that is, between € 1.9 and 2.3 billion) and fund disbursements should stabilise around € 1.8 billion as seen in 2013. The Bank's "loan and project financing policy" was accordingly revised in November 2013, still pursuing conservative risk management orientation, and regulatory framework adjusted in the light of evolving regulatory standards (Basle III and IFRS[13]). Various stress-tests were carried out and support the new framework, provided that the economic context does not deteriorate significantly.

3.3 Long-term vision and proposals by the Governor

31. In a highly unstable environment, the Bank's development plans realistically cover a shorter time span than before. However, the Governor's mission is also to project a longer term vision for the future. This vision was set out in the electoral platform of the current Governor (in 2011) and remains a key benchmark guiding the Bank's development.

32. The "Towards a stronger Bank" vision statement reaffirms the mission of "contributing to a socially cohesive and sustainable Europe in the 21st century". It insists on continued adjustments in governance so as to draw maximum strength from the Bank's comparative advantages. By far the most important asset for the CEB is its close links with the Council of Europe, also as reflected in the Bank's title. This is what

[12] Countries with the lowest GDP per capita (over 2009-2011) score 4 points (Republic of Moldova, Georgia, Albania, Bosnia and Herzegovina, Serbia, "the former Yugoslav Republic of Macedonia", Montenegro, Bulgaria and Romania), followed by those scoring 3 points (Turkey, Latvia, Lithuania, Croatia, Poland, Hungary, Estonia, Slovakia, Czech Republic, Malta, Portugal, Slovenia and Greece). Other countries score 2 points (Iceland, Cyprus, Spain, Italy, San Marino, Holy See, Ireland, France, Finland, Belgium and Germany) or 1 point (Sweden, Denmark, Netherlands, Liechtenstein, Switzerland, Norway and Luxembourg). Countries with 1 point got no new project financing in the last four years.

[13] IFRS = International Financial Reporting Standards.

distinguishes the CEB from other development banks and what should further fuel the complementarity of the two institutions' work. Efforts should continue to convince outsiders to join the partial agreement.

33. The main challenge is and will remain making more precise social targeting of projects feasible, with emphasis on project quality, the blending of grants and loans, as well as good management of risks and uncertainties. It entails enhanced cooperation on capacity building with both borrowers and financing partners (such as the European Commission, the European Investment Bank (EIB) and the European Bank for Reconstruction and Development (EBRD)).

34. The Bank's mission would be greatly served by increased visibility. Building on past steps, the CEB shall therefore continue improving its communication (external and internal) and public relations, including with parliamentarians. Dialogue with member countries (governmental and non-governmental actors) is particularly important in sharing information, expectations and ambition for the Bank's future. In short, the aim is to make the Bank "more relevant, transparent and effective to the benefit of all stakeholders".

35. As rapporteur, I appreciated a series of concrete steps in that direction. These concern mainly:

- the internal restructuring (such as the creation of the Directorate for Human Development and Internal Services composed of the Directorate for Human Resources, the Department for Information Technology and the Department for General Facilities and Security, as well as new Corporate Social Responsibility Department, a stronger Internal Audit Unit and the Office of the Chief Compliance Officer) to streamline the Bank, make it more efficient and better deal with risks and compliance;
- increased attention to, and concentration of, capacities on European cooperation and cooperation with other multilateral development banks through the creation of a cross-directorate Committee for European Cooperation chaired by a Vice-Governor and the creation of the Directorate for European Cooperation and Strategy;
- the adoption of a revised prudential framework (based on recommendations from the *Banque de France*, new Basel III requirements on capital adequacy, leverage and liquidity, and new methodologies applied by the rating agencies) and adjustments in development plans;
- increased attention and adaptation to changes in the regulatory environment which could impact the CEB's business model;
- the introduction of a two-pronged approach for the better social targeting of new projects while preserving focus on target countries;
- new non-lending services;
- the transformation of the Selective Trust Account into the Social Dividend Account;
- the signature of a memorandum of understanding with the EBRD;
- a solution for keeping the essential functions of the secretariat of the partial agreement in Strasbourg;
- improvements in the social climate within the Bank;
- enhanced dialogue with the Bank's shareholders (through the Governing Board and the Administrative Council) including the discussion on the challenges to the Bank's strategy and the field visits of projects organised for Board members;
- more attention paid to internal and external communication (CEB Info newsletter and the strengthening of the Communications Department) in a spirit of transparency and accountability;
- better information on projects: loan documents have been restructured and include an executive summary called "The loan and its social value" which ensures better and more transparent information on the project's social value for the Administrative Council which approves the loan. The Secretary General of the Council of Europe continues to issue an opinion as to admissibility based on the project's conformity with the political and social aims of the Council of Europe.

We shall look at these and related issues in the next chapter.

4. Structure and governance: developments, challenges and response

36. Times are tough and the economic storm is not over. Many Europeans keep on struggling to survive and entire countries are grappling with setbacks in development. Their capacities are weaker – in need of stimulus – to embrace a new, more virtuous development cycle. The CEB has also been challenged to change so as to adapt to rapidly evolving external circumstances. However, reforming internal structures and governance takes time. If there were more trust and consensus within and between the Bank's top bodies, as well as in relation to other Council of Europe bodies, further progress could be made.

37. As my fact-finding discussions with members of the Governing Board have shown, there is concern with the speed of progress in reforming governance. After several years of deliberations, there are still disagreements among members: some opt for a grand package deal along the lines of "nothing is agreed

until everything is agreed" (like at the WTO over the Doha round – with limited results after years of talks); while others would rather see a graduated approach. Yet discussions on 'unresolved governance issues' should eventually produce results, based on greater trust among Governing Board members and their shared sense of common purpose.

38. In my view, breaking the deadlock requires a fresh look at the CEB's key strengths versus weaknesses and new, future-oriented ideas on the table. Some of those ideas should come from the broad field of the Council of Europe's work. The Parliamentary Assembly, the Congress of Local and Regional Authorities and their members, too, could propose bankable social projects to help advance the Organisation's values on the ground. However, they need more information and more regular contacts with the Bank. A CEB stand during the Assembly's and Congress sessions could present information about the Bank, its working methods, ongoing projects and potential for action, notably in priority countries. In this context, it would be helpful to clarify the external representation of the CEB and bring it in line with other international financial institutions.

39. Many of my interlocutors in assessing the Bank's work noted the heaviness of its governance structure in relation to the size of the institution.[14] Leaner decision-making bodies could ensure a more efficient decision process and enhance the Bank's responsiveness to a changing environment. This might also save some resources that could in turn be channeled to reinforcing direct project management capacities within the Bank and among borrowers. Establishing a Board of Directors with reduced yet balanced membership – as recommended by the Strategic Review – remains one possible option that could still be worth considering for the future.

40. Any structural changes in the Bank's governance are intrinsically linked to the voting system, which is complex, and can sometimes be frustrating to the shareholders of the Bank. It has too often slowed down or blocked decision making, which is not in the general interest of the Bank. I wish to encourage members of the Governing Board to reconsider proposals for lowering the majorities required for decisions on the appointment of top officials.

41. From the angle of corporate social responsibility, the CEB continues its regular self-assessment by publishing annual dedicated reports and giving them a prominent place on the Bank's website. Moreover, from 2012, the Annual Report of the Governor includes a separate section on governance and corporate responsibility. This valuable form of communication is addressed to the general public to explain the Bank's mission of socially and environmentally sound financing and how commercial activity is reconciled with the collective interest of sustainable development. As this approach draws on the Council of Europe values enshrined in the Human Rights Convention and the European Social Charter, it could be stated more prominently in annual reports.

42. Turning to the challenges of implementing the Bank's new development plan for 2014-2016, it will be interesting to see how innovative investments accompany prudent banking. Member States have squeezed themselves into the austerity trap and the CEB was pushed into a tighter prudential framework – a genuine "straight jacket" on social ambitions. If public-private partnerships seem to be a luring option, prudence is called for. This is because experience in various European countries shows that public authorities and taxpayers often get ripped off on costs over the longer term, whilst profits and rents for the private sector partners can be exorbitant, with contracts being covered by excessive commercial secrecy and lack of accountability.

43. Regarding staff policies, the current Governor inherited a setup with a certain number of regulatory rigidities and a rather poor social climate. Before his arrival, following repeated signals of malaise among staff members, a survey on staff motivation, engagement and well-being at work was carried out by an external consultant (at about the same time as a similar study was done at the Council of Europe). I am confident that changes have been introduced in a careful and responsible manner, with transparency and fairness for recruitments, promotions and departures being key aims of the process. A new staff survey could be useful to assess progress. Since 2012, a mediator's function was put in place and rules on various allowances were clarified.

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[14] At the IMF, for instance, with 188 member countries, the Executive Board counts some 24 directors representing countries or groups of countries. The EBRD has an in-house Board of Directors with 24 seats representing 64 shareholder countries plus the EU and the EIB. At the CEB, with 41 member countries, the Administrative Council and the Governing Board have 41 members each.

5. Conclusions and recommendations for future work

44. The CEB’s business model has been challenged by a difficult economic and financial environment. The Bank therefore needs to persevere in fine-tuning its activities, structures, working methods and strategic orientations. It has to do so in order to respond more effectively and more rapidly to radical changes in its environment and demands from member States. It should further maximise the social added-value of its projects, its comparative advantage and focus. In particular niche activities – sectoral ones (like prison infrastructure and services, small-scale health sector projects) and geographical ones (such as non-EU countries in South-Eastern Europe) – should be expanded.

45. There is much room for further strengthening the CEB’s links with the Council of Europe, such as in making contributions to supporting various ongoing campaigns, and cooperation with the EU towards strengthening solidarity mechanisms on the ground, in particular with more co-financing in favour of youth employment, Roma integration and housing for vulnerable population groups through projects developed within the Bank’s mandate. Important momentum was created by the changes introduced recently in terms of social screening and the quality of projects. The potential for going even more social, including via further strengthening of the cooperation with the Council of Europe, ought to be tapped without affecting the Bank’s financial stability and position on the market. Complementarities between the CEB, the EIB and the EBRD should be fully exploited and supported by the member States for boosting project resources, management and use of best practice.

46. For reforms to succeed and in order to fully tap the Bank’s potential, all Governing Board members have to contribute towards change and put aside some of their vested interests. The governing structure could be streamlined and the voting system simplified for the sake of greater balance, cost-efficiency and more flexible decision-making. The evaluation and project support functions could further be strengthened, not least by investing more in field visits, technical advice and controls. There is a wealth of creativeness and resources in the Bank and this constructive power should be optimised to enhance the CEB’s ambition for the future.

Appendix

For the **summary on the Bank's functioning, resources and management structure,** please refer to the CEB's website: http://www.coebank.org .

Key figures on CEB activities and projects in 2010-2013

Table 1: **Key figures on CEB activities** (in million euros; data for the end of each year)

	2010	2011	2012	2013*
Loans disbursed during the year	**1 782**	**1 855**	**1 584**	**1 845**
• of which **in target countries**	1056	1 105	989	937
Projects approved during the year (volume)	**2 267**	**2 110**	**1 798**	**2 274**
• of which **in target countries**	1 259	1 290	903	1 101
Loans outstanding	11 988	12 075	12 131	12 582
Own funds (after allocation of profits)	4 987	6 491	7 116	7 320
Subscribed capital	3 303	4 953	5 466	5 472
Paid-in capital	370	554	612	612
General reserve**	1 687	1 613	1 661	1 784
Profit	115.9	106.9	120.2	111.3
Social Dividend Account (available at 31/12)	34.5	31.7	36.3	30.8

* Figures for 2013 are provisional and not yet audited.
** Before allocation of profit

Table 2: **CEB projects approved by sector (2010-2013),** in thousand euros

Sector	**2010, amount** and **%**		**2011, amount** and **%**		**2012, amount** and **%**		**2013,* amount** and **%**	
Social cohesion	**1 125 830**	**49.7**	**1 193 650**	**56.6**	**1 411 069**	**78.5**	**1 702 109**	**74.9**
- Aid to refugees, migrants and displaced populations	-	-	10 000	0.5	70 000	3.9	61 500	2.7
- Social housing	342 000	15.1	318 900	15.1	221 800	12.3	300 000	13.2
- Job creation	400 000	17.7	585 500	27.7	825 519	45.9	1 141 942	50.2
- Urban and rural modernisation	383 830	16.9	279 250	13.2	293 750	16.3	198 667	8.8
Managing the environment	**570 000**	**25.1**	**460 750**	**21.8**	**78 600**	**4.4**	**53 000**	**2.3**
- Natural disasters and preventive action	250 000	11.0	270 000	12.8	-	-	-	
- Protection of the environment	315 000	13.9	180 250	8.5	61 800	3.4	53 000	2.3
- Protection/restoration of cultural heritage	5 000	0.2	10 500	0.5	16 800	0.9	-	
Public infrastructure with social vocation	**326 500**	**13.5**	**455 700**	**21.6**	**308 050**	**17.1**	**518 900**	**22.8**
- Education and vocational training	228 200	10.0	207 500	9.8	-	-	265 900	11.7
- Health	162 810	7.2	129 200	6.1	256 250	14.3	173 000	7.6
- Infrastructure for administrative and judicial public services	180 540	8.0	119 000	5.6	51 800	2.9	80 000	3.5
Total	**2 267 380**	**100**	**2 110 100**	**100**	**1 797 719**	**100**	**2 274 009**	**100**

* Figures for 2013 are provisional and not yet audited. As from November 2013, support for MSMEs (micro-, small and medium sized enterprises) became a separate line of action.

Table 3: CEB <u>loans approved</u> by country (2010-2013), in million euros;
target countries are marked in grey and biggest amounts in bold

Country	2010, amount and %		2011, amount and %		2012, amount and %		2013, amount and %	
Albania	-	-	-	-	-	-	-	-
Belgium	**275**	**12.1**	**270**	**12.8**	**215**	**12.0**	**200**	**8.8**
Bosnia & Herzegovina	-	-	9.2	0.4	61	3.4	70	3.1
Bulgaria	25	1.1	30	1.4	10	0.6	30	1.3
Croatia	6.5	0.3	**155**	**7.3**	50	2.8	**100**	**4.4**
Cyprus	**265**	**11.7**	-	-	-	-	-	-
Czech Rep.	-	-	**100**	**4.7**	-	-	50.0	2.2
Denmark	-	-	-	-	-	-	-	-
Estonia	-	-	-	-	-	-	-	-
Finland	**100**	**4.4**	-	-	-	-	**110**	**4.8**
France	**250**	**11.0**	**200**	**9.5**	**250**	**13.9**	**307.9**	**13.5**
Georgia	-	-	60	2.8	11.7	0.7	30.9	1.4
Germany	***57.5***[1]	***2.6***	-	-	**190**	**10.6**	**100**	**4.4**
Hungary	**125**	**5.5**	**150**	**7.1**	-	-	76.5	3.4
Iceland	-	-	-	-	-	-	-	-
Ireland	**125**	**5.5**	-	-	-	-	41	1.8
Italy	-	-	-	-	-	-	6	0.3
Latvia	-	-	-	-	-	-	-	-
Liechtenstein	-	-	-	-	-	-	-	-
Lithuania	-	-	-	-	-	-	-	-
Luxembourg	-	-	-	-	-	-	-	-
Moldova	-	-	13.4	0.6	-	-	39	1.7
Montenegro	25	1.1	-	-	-	-	10	0.4
The Netherlands	-	-	-	-	-	-	-	-
Norway	-	-	-	-	-	-	-	-
Poland	**302.4**	**13.3**	**300**	**14.2**	**270**	**15.0**	**206.7**	**9.1**
Portugal	**100**	**4.4**	-	-	-	-	-	-
Romania	-	-	**100**	**4.7**	**80**	**4.5**	75	3.3
Serbia	67	3.0	**138.5**	**6.6**	35	1.9	20	0.9
Slovak Republic	50	2.2	**100**	**4.7**	**135**	**7.5**	80	3.5
Slovenia	40	1.8	-	-	-	-	95	4.2
Spain	**108**	**4.8**	**350**	**16.6**	**240**	**13.4**	**408**	**17.9**
Sweden	-	-	-	-	-	-	-	-
Switzerland	-	-	-	-	-	-	-	-
"the former Yugoslav Rep. of Macedonia"	46	2.0	34	1.6	-	-	8	0.4
Turkey	**300**	**13.2**	**100**	**4.7**	**250**	**13.9**	**210**	**9.2**
Total	**2 267.4**	**100**	**2 110.1**	**100**	**1 797.7**	**100**	**2 274.0**	**100**

[1] This included € 7.5 million for the final benefit of target countries.