DOCUMENT OF THE EUROPEAN BANK
FOR RECONSTRUCTION AND DEVELOPMENT

STRATEGY IMPLEMENTATION PLAN
2018 - 2020

As approved by the Board of Directors

EXECUTIVE SUMMARY

The Bank's Strategic and Capital Framework (SCF) 2016 to 2020 set the Bank the goal of supporting its countries of operations in their efforts to improve their economic prospects through re-energising the process of transition to well-functioning market economies. Over the two years that the SCF has been in place, the Bank has made significant progress in helping countries on their path to transition. In addition, it has made substantial advances in an ambitious programme of internal renewal.

This third Strategy Implementation Plan (SIP) of the current SCF period sets out how the Bank intends to continue to pursue its strategic objectives over the period 2018 to 2020. In the course of 2018 – as the mid-point of the SCF period is reached – a review by Management of the Bank's delivery of the SCF will be undertaken to inform future planning.

Progress in 2017

The SIP2017 to 2019 noted that high levels of economic and political uncertainty at both the local and broader geo-political levels made the Bank's work ever more relevant, though more difficult. This pattern of uncertainty has persisted through the year and continues. Despite the challenges, the Bank is performing well and fulfilling its goals. The Transition Impact of the Bank's newly approved and existing projects is at historically high levels. The number of projects – a key determinant of the Bank's ability to make an impact – is running at a similar level as in 2016, although with a smaller average project size.

Investment projects, of course, only capture part of the Bank's contribution to transition impact in our countries of operations. In line with the ambitions of the SCF, the Bank's transition delivery is increasingly broadly based, effectively using a combination of policy tools, technical cooperation and investments. The Bank's multi-year priority investment in policy capability is bearing fruit. There is a greater emphasis on policy goals across the Bank's analytical work and operations, including in country strategies; cross departmental objectives, and project design. Further highlights in the course of the year include accelerated progress towards the goal of reaching 40% of Annual Bank Investment in projects related to Green Economy Transition and progress in the mainstreaming of gender in the Bank's project work and its culture.

This year has seen the revised transition concept approved in late 2016 applied in the Bank's work. With its focus on the key six dimensions of the development of a well-functioning, sustainable market economy, the revised concept is closely aligned with the Sustainable Development Goals, the COP21 agenda and Financing for Development. As a result, it strengthens EBRD's positioning within the global financial architecture. Work is ongoing to embed the six transition qualities into the Bank's work and systems. As anticipated, the increased emphasis on country context and the analytical clarity provided by the transition qualities used, for example, in the updated country diagnostic process, is increasing the Bank's responsiveness. The greater precision of the concept combined with increased standardisation in project design will support better measurement of the Bank's impact. In turn, this will allow the Bank to demonstrate more effectively how its work in delivering its transition mandate contributes to the fulfilment of the Sustainable Development Goals.

The SIP 2018 to 2020

This Strategy Implementation Plan is a natural continuation from its predecessor, testament to the robustness of the rolling planning process. This continuity reflects also a substantially unchanged external environment, as well as the delivery of the Bank's programme of internal change and reinforcement. It also reflects the Bank's fundamental strength. Transition impact is being maintained at near record levels; investment activity is in line with the Bank's ambitious goals; robust financial results and increasingly solid capitalisation underpin financial sustainability and the 'flat budget' framework, reaffirmed in this document, is moderating cost increases. Challenges, however, remain to be addressed.

Optimising Transition Impact

The Bank's work is increasingly driven by its country strategies. Through combining greater analysis of countries' transition needs and opportunities with a clear assessment of the Bank's capacity to support the process of change, the Bank is increasingly well equipped to support the re-energising of transition. Naturally, the overall pace and delivery of the Bank's activities is dependent on a conducive business and policy environment. As highlighted in last year's SIP the Bank's annual activity is inevitably heavily concentrated in a small number of relatively large economies with over 60% of Annual Bank Investment so far in 2017 in five countries and the smallest fifteen accounting for less than 5%. Despite efforts to diversify, aggregate Bank activity is vulnerable to changes in any of these countries. Consistent with the assessment made in the SIP2017-19 uncertainty persists in a number of these countries, which, depending on the turn of events could lead to a potentially wide variance in both investment and policy activity.

The projections contained in this SIP maintain the ambition established in the SIP2017-19, which saw a rising trend in the top end of the Bank's Annual Bank Investment range. Achieving the top end of the range is dependent on a number of factors – notably pricing and risk – being favourable. The level of uncertainty leads to a relatively wide range being proposed for 2018. These projections assume that the guidance of Directors concerning the presentation of projects in Russia remains unchanged, and that the welcome addition of Lebanon as a country of operations and resumption of activity in Uzbekistan contributes only modestly to activities during the start-up phase.

Securing Financial Sustainability

Transition is the Bank's primary objective, yet the Bank must also be financially sustainable. Indeed, the very ability of the Bank to have impact and meet the needs of countries of operations requires ongoing positive net income to support both capital growth and grant provision through the Shareholder Special Fund.

The Bank is financially strong and has recently had its unqualified triple-A credit rating reaffirmed by all the ratings agencies. The analysis presented in this SIP further shows that the Bank is increasingly strongly capitalised with capital growth now projected to be broadly in line with the base case levels assumed in the SCF. In short, the Bank does not face an immediate capital constraint. The projections show that Bank can support the ambitions presented here and withstand stress events, whilst still having the capacity to support additional operational activities should opportunities be available in the Bank's countries of operations.

The Bank does not take its financial strength for granted, the focus maintained in 2017 on containing costs and increasing income generation will continue.

Creating a leaner and more efficient organisation

Shareholders expect the Bank to operate efficiently and deliver value for money. To support this an Operational Effectiveness and Efficiency programme – the largest change programme in the Bank for many years – was initiated in 2016 with implementation starting in 2017 and continuing in the period covered by this SIP. The programme has already started to yield concrete benefits, for example: reduced process burdens through clearer and more extensive delegation; enhanced country strategies produced more rapidly, and increasingly automated processes for assessing the transition impact of projects. The Bank is committed to continuous improvement.

The financial goals for the programme have been delivered for 2017 as planned. However, future savings are not now expected to materialise as initially projected. This SIP thus presents a revised profile of the programme over the remainder of the SCF period which provides context for the Board of Directors' consideration of the 2018 Budget. Despite the challenges in achieving future savings – and consistent with the objective of ensuring the Bank is lean and efficient and previous commitments – the 2018 Budget is no higher than the level which existed in 2016 before compensation related adjustments. In line with earlier understandings, the material changes in the Bank's scope caused by Lebanon becoming a country of operations and the resumption of activity in Uzbekistan are considered as additions to the budget baseline.

2018 – Goals and Resources

The business objectives for 2018, set out in the Corporate Scorecard are:

- Expected Transition Impact floor for new projects set at 60;
- Portfolio Transition Impact floor set at 65;
- Number of operations within a range of 360 to 400
- Annual Bank Investment within a range of €8.1 to 9.0 billion;
- Annual Mobilised Investment floor set at €0.8 billion, with a floor for combined annual Bank and mobilised investment set at €8.9 billion;
- Annual disbursement range of €5.4 to 6.7 billion; and
- A level of the three year rolling average of the Return on Required Capital of at least 3.5%.

The Scorecard also contains the Composite Performance Assessments of the Bank's work for each of the six transition qualities. These objectives do not constrain the Bank's ambition. Throughout any year, the Bank always responds to the prevailing opportunities. Should the business and transition environment prove more favourable, it may be possible to exceed these objectives to deliver more fully on the Bank's mandate, including, amongst others, higher levels of Green, equity and mobilised investment.

On the basis of the context provided by this SIP the 2018 Corporate Scorecard was approved and the Bank's total Administrative Expense Budget for 2018 is £359.5 million (€399.0 million).

STRATEGY IMPLEMENTATION PLAN 2018 -2020

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ABBREVIATIONS

ABI	Annual Bank Investment
AMI	Annual Mobilised Investment
ASB	Advice for Small Business
BP	Business Plan
BAAC	Budget and Administrative Affairs Committee
CA	Central Asia
CAP	Capital Adequacy Policy
CEB	Central Europe and the Baltics
COP	Conference of the Parties
CPA	Composite Performance Assessment
CSG	Client Services Group
EEC	Eastern Europe and the Caucasus
ESD	Environment and Social Department
ETC	Early Transition Country
ETI	Expected Transition Impact
FTE	Full Time Equivalent
FV	Fair Value
GCF	Green Climate Fund
GET	Green Economy Transition
IFC	International Finance Corporation
IRR	Internal Rate of Return
LC2	Local Currency and Capital Markets
MSME	Micro, Small and Medium-sized Enterprise
MDB	Multilateral Development Bank
NPL	Non-Performing Loan
OCCO	Office of Chief Compliance Officer
OE&E	Operational Effectiveness and Efficiency
PPP	Public Private Partnership
PTI	Portfolio Transition Impact
RAROC	Risk Adjusted Return on Capital
RoRC	Return on Required Capital
RO	Resident Office
SCF	Strategic and Capital Framework
SEFF	Sustainable Energy Financing Facilities
SEE	South East Europe
SEMED	Southern and Eastern Mediterranean
SIP	Strategy Implementation Plan
SME	Small and Medium-sized Enterprises
SPM	Strategic Portfolio Management
SSF	Shareholder Special Fund
TC	Technical Cooperation
TFP	Trade Facilitation Programme
VP3	Vice Presidency, Policy and Partnerships
WAPD	Weighted Average Probability of Default

STRATEGY IMPLEMENTATION PLAN – 2018 to 2020

1. INTRODUCTION

The EBRD's strategic objectives and operational directions are set out in the Strategic and Capital Framework 2016 to 2020[1] (SCF), formally approved by the Bank's Governors at the 2015 Annual Meeting. This Strategy Implementation Plan (SIP) is the third three year rolling plan of the current SCF period. It provides an account of the Bank's approach to delivering its transition purpose from 2018 to 2020 covering objectives; envisaged policy and investment activities; use of capital and required resources. All these elements provided the context for the consideration of the Bank's annual Budget and Corporate Scorecard for 2018.

The overarching theme of the SCF was that the Bank should support its countries of operations in 're-energising transition' with a particular emphasis on addressing needs in the geographic areas where transition is less advanced. In achieving this, the SCF recognised that Bank's instruments, focus and skill set would have to evolve. The overall framework is most succinctly summarised in Box 1, taken from the SCF itself. Progress towards many of these goals will be highlighted in this document.

Box 1: The Bank in 2020

The Bank's operational profile will include:

- An even higher proportion of activities that incorporate sustainable energy and resource efficiency components and considerably stepped-up operations in energy security
- A comprehensive suite of solutions to support SMEs, entrepreneurship and innovation
- An active and comprehensive programme of local currency and capital market development
- A strong infrastructure project preparation offer together with increased financing for sustainable infrastructure projects, within and across borders
- A wide range of products that can address the evolving transition needs of its countries and clients—notably, a higher proportion of equity investments

The Bank will, across all its operations:

- Have a significant, structured policy dialogue capacity, leveraging its project work and aimed at sector reform and institutional and governance improvements
- Fully mainstream inclusion and gender objectives
- Mobilise significant cross-border capital and investments from both traditional and non-traditional sources
- Further strengthen results orientation and alignment of objectives and apply lessons learned.

The priorities will be implemented through future annual Strategy Implementation Plans with continued efforts to manage both existing projects and new commitments to pursue transition impact whilst balancing, in the portfolio, risks, returns and costs to ensure financial sustainability. Over the SCF period, the Bank will maintain its strategic orientation to move progressively towards countries and regions within countries that are less advanced in transition and, by 2020, will conclude its engagement in new operations in Cyprus and Greece in accordance with Resolutions 173 and 177.

In the implementation of the Bank's strategy, each successive SIP takes its predecessor as a starting point. The current external environment is broadly similar to that which prevailed at the time of consideration the SIP2017-19. Although there are some signs of a modest pick-up in growth across the Bank's region, economic circumstances continue to be challenging with investment – and especially Foreign Direct Investment - at relatively low levels. In addition, global and local political developments increase uncertainty in many countries. Both economic and political uncertainty can limit opportunities for the Bank to support transition. The impact of these uncertainties on the Bank's planning and delivery is amplified when encountered in Bank's larger countries of operations.

[1] Report of the Board of Directors to the Board of Governors 2015 Annual Meeting: Strategic and Capital Framework 2016 – 2020.

Internally, the picture is again broadly similar to that outlined in the SIP2017-19. The strengthening of the Bank's capability highlighted in previous SIPs has continued and is having an effect. Amongst the priority areas for investment identified in SIP2016-18, additional resources for Green Economy Transition (GET) activities are reflected in the growing share of the Bank's business activity in this area. Similarly, the symbiotic relationship between policy and investment activity in delivering the Bank's transition mandate is increasingly recognised within the Bank and reflected in more clearly articulated goals in Country Strategies and implemented through specific objectives fully shared by investment and policy departments.

Multi-year commitments have been made with respect to the Bank's Operational Effectiveness and Efficiency programme. To date, the programme is broadly on track, and in 2017 created the budgetary capacity anticipated. Its implementation and impact are also integral to this SIP, both in terms of the improvement of the Bank's systems and internal organisation and its ongoing financial effect. However, significantly changed projections for its budgetary impact are outlined in this document reflecting adjustments to the Programme's implementation and savings profile.

Geographically, the Plan assumes that the guidance of Directors concerning the presentation of new projects in Russia remains unchanged. There has been material change in the scope of the Bank's activities over the year as Lebanon has become the Bank's latest country of operations and activity has resumed in Uzbekistan. As foreshadowed in the SIP2017-19 the budgetary impact of these changes are treated as additions to the Bank's budgetary baseline.

As a result, this SIP shows:

- A pattern of **transition delivery** through investment and policy activities which is similar in scope and distribution to that contained in SIP2017-19, including continued limited opportunities in equity;
- Enhanced **financial sustainability** with a projection for capital utilisation which shows the Bank able to fully support the proposed Plan and withstand stress events whilst retaining the capacity to increase investment in support of shareholders' objectives; and
- A continuing striving for **efficiency** with the modernisation of the Bank's processes, procedures and systems supporting an Administrative Expense Budget (excluding compensation increases) for 2018 no higher than the 2016 level, as committed to in the SIP2017-19.

The structure of the document is as follows:

- Section 2 sets out the evolution of the control parameters from the SCF over the period covered by the SIP, compliance with which in the first year of the Plan is a necessary condition for consideration of the 2018 Budget. The section highlights changes approved by the Bank's Board of Governors to the control framework due to the projection of the Bank's Cost to Income ratio for 2018. The Corporate Scorecard for 2018 is also presented;
- Section 3 provides a brief overview of the economic and political trends in the Bank's region which form the backdrop to the policy and business opportunities which condition the Bank's work in the coming three years;
- Section 4 sets out the range of objectives to be pursued by the Bank through implementation of its country strategies, reflecting the revision of the transition concept and highlighting particularly objectives requiring the integration of policy and investment activities;

- Section 5 gives an overview of the Bank's activities to deliver its transition objectives. It sets out how the Bank's strategic directions are combined with the business and policy delivery opportunities and its financial objectives to shape its overall activity in countries of operations. The section goes on to describe investment activity together with the level of anticipated grant support over the period covered by the SIP;
- Section 6 contains the financial and capital utilisation projections implied by the assumed investment activity. It considers the financial robustness of the Bank in the face of economic stress. For 2018, a new objective is included in the scorecard to better measure the Bank's profitability and long term financial health. This section also sets out the 2018 borrowing programme;
- Section 7 provides detail on the Bank's Operational Effectiveness and Efficiency programme. It outlines briefly the extent of the work being undertaken together with a revised investment and saving profile;
- Section 8 presents the resourcing trends for the period covered by the SIP together with the Administrative Expense Budget for 2018.

2. THE CONTROL FRAMEWORK AND CORPORATE SCORECARD

In addition to setting the high level objectives for the Bank, the Strategic and Capital Framework set six 'control parameters' for key aspects of the Bank's performance to 2020. Together these defined the boundaries within which the Bank should work during the period. These control parameters consist of:

- Minimum levels for the Bank's transition delivery through its projects at approval and throughout their life to ensure that the Bank's core purpose was adequately fulfilled at all times;
- Maximum levels of capital utilisation as measured both on a statutory basis and through the Bank's Capital Adequacy Policy to ensure the Bank's basic financial soundness;
- Maximum levels for the five year rolling average of each of the Bank's Cost to Income ratio and the share of Staff Costs in Total Costs to support continuous cost efficiency.

The trends in these parameters play an important part in guiding the Bank's work. Specifically, compliance with the various limits in the first year of the period covered in any SIP is a precondition for the approvals of that year's Corporate Scorecard and Budget.

This section summarises the projected levels for each of the parameters over the period 2018 to 2020. As anticipated in the SIP2017-19, the projections for the Cost to Income ratio are above the limits set in the SCF for the years 2018 and beyond. On the recommendation of the Board of Directors the Board of Governors has approved a revised limit and new procedures for ensuring ongoing cost effectiveness in the Bank.

2.1 Transition Parameters

Floors are set for the average quality of the Bank's projects at their initial approval (the Expected Transition Impact (ETI)) and over their lifetime (the Portfolio Transition Impact (PTI)) as measured through the Bank's internal systems.

These floors require the Bank to achieve levels of ETI above 60 and PTI above 65. At the end of September, the Bank was operating well above these floors, with levels standing at 67.6 and 70.2 respectively.

The Bank does not produce projections for the future evolution of these measures, but the degree of margin over the floor levels together with the approach taken to project selection give high confidence that these levels will continue to be exceeded in the next year and in future years of the SCF period.

2.2 Capital Parameters

The capital utilisation parameters, designed to ensure that the Bank is financially sound, require the Bank to maintain its level of:

- Statutory capital utilisation below a ceiling of 92%: and
- Utilisation under the Bank's Capital Adequacy Policy of 90%.

Projections across the period covered by this SIP are shown in table 2.1. They show that for the entire period it is anticipated that the Bank will be well below the ceiling level. The underlying calculation of these figures is contained in chapter 6.

Table 2.1: Capital Utilisation Projections 2015 to 2020

	Control Level	2015 Actual	2016 Actual	2017 Estimated	2018 Projected	2019 Projected	2020 Projected
Statutory	<92%	71%	73%	70%	70%	71%	71%
Capital Adequacy Policy	<90%	80%	77%	73%	73%	73%	72%

2.3 Resource Parameters

Two control parameters are also set for resourcing. The first is a ceiling for the five year rolling average of the ratio of the Bank's costs to its realised income. The measure is intended to give incentives to balance both cost control and income generation with the rolling average designed to smooth fluctuations. The SCF set a ceiling on this measure of 33% consistent with the Bank's historical performance and the performance of peer organisations. The second control parameter set a ceiling for the ratio of staff costs to total costs at 70% as a substitute for the previous use of a head count ceiling for managing staff costs.

The projections for the period to 2020 are presented in table 2.2. The table shows that the five year rolling average for the Cost to Income ratio is projected to exceed the ceiling level set in SCF in 2018 and rise further in 2019 and 2020.

Table 2.2: Resource Parameter Projections: 2015 to 2020

	Control Level	2015 Actual	2016 Actual	2017 Estimated	2018 Projected	2019 Projected	2020 Projected
Five year rolling average of:							
Cost to Income ratio	<33%	25.1%	27.5%	30.8%	35.2%	39.1%	42.9%
Staff Cost to Total Cost	<70%	67%	68%	67%	67%	67-68%	67-68%

The reasons for the current projection showing a significantly higher level than the Bank's past experience were examined at some length in the SIP2017-19[2]. In summary:

- The Bank's costs have evolved – and are expected to evolve – in line with the expectations expressed in the SCF and presented in successive SIPs and associated Budgets; but
- Realised income is projected to be lower than past experience. The overwhelming majority of the changed outlook is accounted for by lower actual and projected realised gains from equity, reflecting both lower valuations as a result of the external environment and the realising of historic losses in the portfolio. This has been compounded since projections for interest margins and returns on the Bank's liquidity are both lower than expected previously.

[2] Strategy Implementation Plan 2017-2019.

Projections for realised income in this SIP are higher than in the SIP2017-19 reflecting better than anticipated income performance in the latter part of the 2016 and through 2017. However, the overall conclusion remains that that the Bank's five year rolling average Cost to Income ratio will be above the permitted level in 2018 and for the remainder of the period to 2020.

The Bank has put in place structural actions on both income and costs. On costs, the Organisational Effectiveness and Efficiency programme (OE&E) will deliver full year savings of around 2.5% of the Bank's total budget in 2018. The details of this programme and its financial impact are contained in sections 7 and 8. The Bank has also increased its focus on income generation.

This action will not cause the five year rolling average of the Cost to Income ratio to move below the ceiling level in 2018. The Board of Governors has approved a recommendation by the Board of Directors for a comprehensive overhaul of the calculation methodology, the control levels and governance of the Cost to Income control parameter. Through this, Governors set a ceiling level of the five year rolling average of the Bank's cost to income ratio of 50%. This ratio would be calculated using net income before impairment, including all fair value movements on both Banking and Treasury operations investments, and prior to costs, instead of the current definition based on realised income.

This approach is complemented by an enhanced role for the ratio in the work of the Board of Directors. Through this the Board of Directors will establish its own lower operational ceiling for the five year annual rolling average of the Bank's cost to income ratio of 40%. Should this level be exceeded, Bank Management would present to the Board of Directors an analysis of the causes of the rise in the ratio and appropriate remedial measures to return the cost to income ratio to the target range. The Board of Governors would be informed of the event and actions.

An annual objective, below the ceiling, is also to be set by the Board of Directors which would provide a benchmark for assessing the financial consequences of any new activity. **The level for 2018 is set, consistent with the current projection at 39.7%.**

The effect is to set the level of this parameter at a control level, akin to the other control parameters in the framework. The current level of the parameter is more appropriate for an operational target and the approach has the effect of aligning the operational targets with operational instruments. The combined effect is to increase transparency and maintain, if not enhance, the level of discipline over resources in the Bank. The projections in table 2.3 show that the level for the five year rolling average of the Bank's cost to income ratio will be below the new control level for the entire period covered by the current SIP.

Table 2.3: Proposed Revised Resource Parameter Projections: 2015 to 2020

	Control Level	**2015** Actual	**2016** Actual	**2017** Estimated	**2018** Projected	**2019** Projected	**2020** Projected
Five year rolling average of:							
Cost to Income ratio	<50%	35.7%	32.8%	36.2%	39.7%	34.3%	33.1%
Staff Cost to Total Cost	<70%	67%	68%	67%	67%	67-68%	67-68%

2.4 Corporate Scorecard

The Corporate Scorecard encapsulates, at the highest level, the commitment of the Bank to deliver its mandate. It represents a balance of the Bank's transition, operational, and financial objectives as well as resourcing and organisational goals. The structure of the 2018 Corporate Scorecard remains unchanged from 2017, thus preserving stability.

There is one change within this stable structure. The Bank's financial objective is now set with reference to a floor for the three year rolling average of the return on required capital. Previously the Bank's profitability objective had been to achieve a level of realised profit before impairment within a set range. This indicator will no longer be targeted, but will be tracked within the scorecard. The third indicator in the financial section of the scorecard – the level of the stock of non-performing loans - remains tracked.

The Corporate Scorecard provides the framework within which more detail is presented in the remainder of the paper.

Corporate Scorecard – 2018

	2018	30/09/2017	2017	2016
	BP and Budget	Actual	BP and Budget	Actual
TRANSITION IMPACT				
Expected Transition Impact	**Min 60**	67.6	Min 60	66.7
Portfolio Transition Impact	**Min 65**	70.2	Min 65	70.6
Transition Qualities				
Competitive, innovative economies	**CPA***	**Very Good / Good / Requires Attention**		
Well-governed economies and firms	**CPA**	-		
Environmentally sustainable, green economies	**CPA**	-		
Inclusive, Gender-equal economies	**CPA**	-		
Resilient economies and firms	**CPA**	-		
Well-integrated, connected markets	**CPA**	**-**		
OPERATIONAL PERFORMANCE				
Number of operations	**360-400**	212	360-420	378
Annual Bank investment (€ billion)	**8.1-9.0****	5.1	8.1-8.9	9.4
Annual mobilised investment (€ billion)	**Min 0.8**	0.4	Min 0.8	1.7
Disbursements (€ billion)	**5.4-6.7**	4.1	5.2-6.5	7.8
FINANCIAL PERFORMANCE				
Return on Required Capital (3 year rolling average)	**Min 3.5%**	5.9%	Tracked	3.3%
Realised profit before impairment (€ million)	**tracked**	550	400-600	642
Non-Performing Loan ratio (non-sovereign) (%)	**tracked**	5.5%	Tracked	6.6%
ORGANISATIONAL PERFORMANCE				
Productivity (number of operations based)	**1.7-1.9**	-	1.7-1.9	1.8
Staff Engagement Ratio	**tracked**	-	Tracked	-
RESOURCE FRAMEWORK				
EXPENDITURE				
Administrative Expense Budget				
Euro (million)	**399.0**	282.9	401	465
Pound Sterling (million)	**359.5**	244.5	346	341
Operational Effectiveness and Efficiency Investment***				
Euro (million)	**12.8**	13.2	27.8	
Pound Sterling (million)	**11.0**	11.4	24	

* Composite Performance Assessment
** Up to €0.7 billion in BP2018 fungibility possible once minimum Annual Mobilised Investment is achieved.
******* The OE&E Investment Budget approved in 2017 covers the life of the OE&E programme. The figures here are the estimated available funds carried forward to 2018.

OPTIMISING TRANSITION IMPACT
3. THE TRANSITION CONTEXT

The challenges to which the Bank should respond and its ability to do so are shaped by the economic and political context. This section considers the economic backdrop against which this Strategy Implementation Plan has been developed and the high level challenges for the medium term before turning to the particular financing needs facing the region. Structural reform needs are also touched on.

3.1 Economic trends

Short term outlook

The short term economic outlook for the Bank's region has improved slightly, but remains challenging. After declining for five consecutive years, the average annual growth rate in the EBRD region picked up modestly, from 1.3 per cent in 2015 to 1.9 per cent in 2016. It has remained below the average level achieved in the economies with similar income levels globally for the eighth year in a row and will remain lower than in comparator economies on current projections, as discussed in the *Transition Report* 2017-18.

Average growth is expected to pick up further, to 3.3 per cent in 2017 and before decelerating 2.3 per cent in 2018 as fiscal stimulus wears off in Turkey, the one-off impact of higher social payments in Poland fades away and shortages of skilled labour constrain medium-term growth potential in Central Europe. Russia's economy is projected to return to moderate growth after a cumulative output decline of 3 per cent in 2015-16. Growth is also expected to pick up slightly in Central Asia and Eastern Europe and the Caucasus (EEC) reflecting a stabilisation of commodity prices and resumed growth in Russia. Ukraine's economy returned to growth in 2016, although the pace of recovery is slower than anticipated.

Growth in Central Europe and the Baltic States (CEB) and south-eastern Europe (SEE) is also projected to strengthen, reflecting a pick-up in investment after a dip in 2016 and a number of country-specific drivers. Growth in the southern and eastern Mediterranean (SEMED) projected to increase to around 4 per cent in 2017 and 2018, as a drop in purchasing power of Egypt's consumers owing to high inflation is offset by stronger investment and exports and agriculture rebounds in Morocco and Tunisia.

Medium-term trends and challenges

Growth prospects in the longer term are uncertain. A slowdown in structural reform and a prolonged period of lower investment relative to emerging market peers, as highlighted in the *Transition Report* 2017-18, may weigh on the outlook for growth. These effects are further compounded by increasing demographic pressures in emerging Europe. The external environment creates additional headwinds to growth. These include slower expansion of international trade, moderate growth in the advanced economies and increased economic policy uncertainty in several G7 economies.

Geopolitical tensions in and around the region are a major source of risks to the medium-term economic outlook.

3.2 Financing Needs

Capital flows to emerging markets have remained robust as search for yield in a low-interest rate environment continued. Although the US Federal Reserve raised its funds rate several times, to the range of 1 to 1.25 per cent, the pace of monetary tightening has been, if anything, slower than originally expected.

In the medium term, capital flows to emerging markets, including the EBRD countries of operations, are expected to remain significantly below pre-crisis levels and are likely to fall short of the levels observed in 2010-14, as interest rates gradually rise in the advanced economies and the risk-return balance offered by emerging markets becomes less attractive.

Some progress has been made with resolving non-performing loans (NPL) that burden balance sheets of region's banks and corporates. At the same time, the declines in NPL ratios from their peaks have, on average, been modest and NPL levels remain elevated across much of the EBRD region. In part reflecting this burden, credit growth has remained modest in most countries in the region (with a few notable exceptions that include Turkey).

3.3 Structural reform needs

Recent years have been challenging for reformers across the transition region although the reform momentum appears to have strengthened somewhat in 2017 according to the assessment of transition qualities in the Transition Reform 2017-18. As noted in the previous section, many of the factors identified in earlier Bank analysis[3] that deter market-oriented reforms – such as weak or negative growth, global and regional turbulence and instability, and weak state and public administrations – continue to be present. Some countries, nevertheless, have shown a commitment to improving governance and fostering a better business environment, while others are increasingly recognising the important role the private sector can play in traditionally public-dominated sectors such as infrastructure and energy. On the other hand, a number of countries remain reluctant to undertake reform and face major challenges. This environment circumscribes the ability of the Bank to be effective in supporting reform. Generally, the Bank seeks to work with partners committed to reform and is able to do more where that reform commitment is stronger.

4. ACHIEVING TRANSITION

The Bank's mission is to support its countries of operations in achieving the transition to a sustainable, well-functioning market economy. This section presents the strategic approach for defining, delivering, and monitoring transition impact in two parts:

- Section 4.1 provides a high level summary of the Bank's transition objectives which will be pursued through the implementation of its country strategies during the period covered by the SIP;
- Section 4.2 sets out the specific transition objectives to be assessed through the Corporate Scorecard in 2018.

4.1 Transition Objectives

2016 saw the approval of a revised transition concept to reflect the six key qualities of a sustainable market economy. These qualities incorporate new insights on the role of markets and align with the international community's ambition for the private sector to make major contributions to achieving the 2030 Agenda for Sustainable Development. Consistent with this global outlook, the Bank's ability to achieve its objectives increasingly requires collaboration with other International Financial and regional institutions.

A key tenet of the revised concept has been a greater emphasis on country context in judging the progress towards transition. This insight is made operational through the formulation of country strategies based on an analytical framework which systematically identifies: the needs of the country to progress towards the achievement of the qualities of a market economy (via an assessment of transition qualities and subsequent in-country diagnostic work); the opportunities which may exist for making progress in fulfilling those needs; and the capacity

[3] *Stuck in Transition*: Transition Report 2013

of the Bank to take advantage of those opportunities. This provides a powerful tool for concentrating the Bank's work where it can be most effective.

Box 2: Economic Inclusion Strategy

The Bank launched its first Economic Inclusion Strategy (EIS) at the Annual Meeting in Cyprus in May 2017 as a key instrument for delivering the SCF commitment in this area. The EIS seeks to deepen and strengthen the Bank's distinct private sector led work on inclusion to create economic opportunities for women, young people and populations in underdeveloped regions. It will also gradually and carefully widen its approach to other potential groups such as refugees, ageing populations or people with disabilities based on Country Strategy priorities. This will build on existing successful approaches to skills and vocational training and by exploring new opportunities where inclusion can add value to the Bank's offer to clients.

- To date, the Bank has invested a total of EUR 3.9 billion in 83 projects with inclusive transition impact, primarily in FI and ICA sectors but increasingly also in Infrastructure, and Energy and Natural Resources.
- €14.2 million of donor funds and SSF have been used to supporting inclusion TCs to enable clients to enhance vocational training programmes, establish partnerships with schools and universities, introduce equal opportunities corporate practices, or establish inclusive procurement practices.
- Policy dialogue objectives are being successfully achieved in Jordan, Turkey and Kazakhstan. By creating platforms that bring together policy makers with the private sector, the Bank acts as a catalyst for the establishment of high quality vocational skills standards and dual learning models (such as, apprenticeships or internship standards) at national levels. Strong strategic partnerships with the European Training Foundation, the EU's agency for human capital development in neighbourhood and accession countries, the UN World Tourism Organisation, and others, support this policy dialogue.
- The EBRD's analytical and operational work on economic inclusion is recognised for its innovative approach across key parts of the IFI community. It is regularly presented at major international fora, including the World Bank, UN, EU, OECD and others, and promoted through the EBRD internal and external communications channels.

Using this framework, the Bank's country strategies identify the priorities and objectives, aligned with the six qualities of the revised transition concept that will guide its investments, policy engagements, and advisory work. In addition, under the enhanced and structured approach to policy reform dialogue, the Bank has developed annual priorities for systematic engagement with governments on key policy objectives. With this approach, policy work leverages and reinforces investment impact in a cohesive and structured manner. Given that the country strategy framework rests on local needs, opportunities and the Bank's capacity to deliver on them, it is not expected that investments will be evenly spread across the qualities.

The following sections present a regional overview of the Bank's country strategy priorities and objectives, covering both investment and policy dialogue activities.[4] These objectives are set out in more detail in country strategies.

Central Asia

The Bank prioritises development of more competitive, well-governed, resilient and integrated economies throughout the region. Green and inclusive qualities of transition are targeted in the most recent strategies of Mongolia and Kazakhstan. Policy dialogue focuses primarily on strengthening financial sector resilience, governance (particularly in the energy and banking sectors) and infrastructure.

The Bank promotes **competitiveness** in the region by supporting privatisation and commercialisation (particularly of state-owned infrastructure and utility companies) and improving private sector competitiveness through investment and Advice for Small Businesses (ASB) across the region, notably in the Kyrgyz Republic, Tajikistan and Turkmenistan. In parallel, the Bank promotes operational and financial effectiveness and efficiency of municipal infrastructure and utilities. The Bank also targets the deepening of

[4] Since SIP 2017-2019, six new country strategies have been adopted.

financial intermediation through increased local currency financing of PFIs and issuance of local currency bonds in conjunction with policy advice on financial regulation and new banking products, to improve the **resilience** of the financial sector. Enhancing domestic capital markets, and increasing their transparency, is a policy priority objective Kazakhstan.

To support development of **well-governed** economies and firms, the Bank aims at improving corporate governance through investments complemented by policy engagement to support an investor-friendly environment – for example, by raising the quality of the legal and regulatory environment in the natural resources sectors in Turkmenistan and engagement with investment councils in Kyrgyz Republic and Tajikistan.

The Bank further supports a more **integrated** region by concentrating its activities on developing transport infrastructure, including through commercial solutions such as PPPs, and regional exports. In addition, the Bank engages in policy dialogue to address soft infrastructure such as customs and border procedures. The Bank's recent focus on a **greener** and more **inclusive** region includes its support of renewable energy projects in Mongolia and extending SME credit lines for underserved groups in Kazakhstan.

Central Europe and Baltics

In Central Europe and the Baltics, the Bank focuses on competitive, resilient, and green transition qualities, with an overarching objective to support frontier-level innovation and higher-value-added activities given the advanced economies of the countries in this region.

The Bank aims to bridge the remaining transition gaps in **competitiveness** with a focus on innovative and export-oriented local corporates and SMEs, while helping diversify their sources of financing away from lending and towards equity and other instruments. In Slovenia, this would be complemented by improved corporate governance. To advance a more **resilient** economy, the Bank seeks to strengthen the region's financial sector and develop local capital markets. The Bank also focuses on improving energy security (especially in the Baltics) through diversification of supply, regional energy market integration and the development of local renewable sources. This is supported by energy efficiency investments and policy dialogue. Policy priority objectives include strengthening economic resilience by improving Capital Market regulation, efficiency and accessibility, in Croatia and Poland.

Cyprus and Greece

Competitiveness, integration and resilience provide the fulcrum of the Bank's activities in Cyprus and Greece. To support a more **competitive** economy, the Bank's engagement is centred on addressing the high leverage and operational inefficiencies and new investment funding needs in the corporate sector and improving transport and municipal services with a focus on utilities (through privatisation and investment in PPPs). In Greece, efforts are aimed at enhancing governance standards and supporting with risk capital products a knowledge-economy through innovation and skills. TFP lines, support of FDI inflow and investment in cross border projects will facilitate deeper economic **integration** in the region and beyond.

The Bank prioritises the **resilience** of the financial sector, aiming to assist the restoration of banks' access to capital markets and support market mechanisms to resolve NPLs. The Bank also supports the development of non-bank financial institutions and diversification of sources of funding for local corporates; as well as the restructuring and diversification of the energy market. In Greece, for example, the Bank engages in policy dialogue on a new framework for renewables along with providing financing for private renewable energy providers.

Box 3: Priority Policy Objectives

Over the past two years the setting of priority objectives, drawn from country strategy priorities, to be pursued by policy engagement in concert with investments, has been piloted. The pilot has been successful and fifteen countries are now covered through this approach, which will be further rolled out in future. Highlights include:

- In Kazakhstan, the Bank is working to enhance the regulatory framework for renewable energy, energy efficiency and green finance; and improve national skills standards and equal opportunities in the energy and natural resources sectors.
- Development of local capital markets is a priority in both Croatia and Poland.
- In Belarus, priorities include commercialisation of municipal utilities and implementation of tariff reform; and assistance with preparation of two state-owned banks for privatisation.
- Reform of the natural gas sector, and of state-owned banks and other enterprises, aimed at their commercialisation and future privatisation, are priorities in Ukraine.
- In Albania, the Bank focuses on improvement of Albanian Power Corporation (KESH)'s governance and operational practices, enhancement of tax compliance, and the development of a Green City Action Plan (GCAP) for the city of Tirana.
- Introduction of improved national skills standards in hospitality and tourism, and addressing barriers to female entrepreneurship, are priorities in Jordan.
- In Egypt the Bank works to promote investments in green logistics, and develop a low-carbon roadmap for the cement industry, with a target to reduce the CO_2 impact of the industry by 5 per cent.
- Improving the effectiveness of vocational education and training through private sector engagement and rationalising incentive measures provided to the agricultural sector are priorities in Turkey.

This is part of a continuing effort to strengthen the joint delivery of transition objectives and to provide collective incentives for their achievement. The intention over the period of the SIP is to continue to reinforce the Bank's capacity to undertake policy reform dialogue and to be able to measure its impact and results.

Eastern Europe and Caucasus

In Eastern Europe and the Caucasus, the Bank's strategy priorities are to enhance the region's **competitive** and **resilient** qualities, in addition to its support of a **well-governed** economy in four out of the six countries. For all three qualities, investment is complemented by extensive policy dialogue activities.

The Bank aims at enhancing private sector **competitiveness** across all countries, facilitating technology transfer and the development of a technology infrastructure in Georgia, and in Ukraine, providing emergency financing to corporates and promoting privatisation. In Armenia, Belarus and Moldova the Bank emphasises improving infrastructure and public utilities through direct (co-) investments whilst engaging in policy dialogue to promote commercialisation of municipal utilities. The Bank further focuses on strengthening **governance**, particularly through improving the region's business and investment environment. Activities range from support for investment councils (Armenia), investor councils and competition authorities (Georgia, Moldova), and the law on public procurement (Moldova).

The Bank aims to build **resilience** by supporting the development of local capital markets, enhancing the non-banking financial sector and increasing the use of LCYs. Specific country foci include consolidation of the banking sector (Azerbaijan, Ukraine) and support for de-dollarisation in Georgia; while restructuring of the Moldovan banking sector, in concert with the World Bank and IMF, is a key policy priority. Energy resilience is prioritised in four out of six countries in the region (Armenia, Azerbaijan, Moldova and Ukraine). The Bank has also initiated its **inclusion** agenda by focusing on narrowing the skills mismatch in Georgia.

Southern and Eastern Mediterranean

The Bank's priorities in SEMED focus mainly on the competitive, resilient and inclusive qualities of market economies. To develop **competitive** economies, key objectives of the Bank are to facilitate SME's access to finance across the region and to promote best operational and management practices. Activities include direct and indirect financing of SMEs accompanied by business advisory services and important engagement in policy dialogue activities. Improvement of operating practices of public utilities and the quality of infrastructure are further priorities.

The Bank targets strengthening **resilience** by supporting the development of both a sustainable energy sector and more diversified domestic financial markets.

The Bank's **inclusion** agenda is emphasised in all three existing SEMED country strategies.[5] In Egypt, Jordan and Morocco, the Bank aims at increasing economic opportunities for women and youth; and in Morocco, at providing equal access to public services in remote regions. In Jordan, providing employment and access to services for refugees is also a priority.

Support for **green** market economies is an objective in Jordan and Egypt, where the Bank will offer energy efficiency credit lines through local banks in cooperation with other IFIs and engage in policy dialogue to promote legislation to support investment in energy efficiency and renewable energy. Green and competitive transition qualities are also the priority for policy objectives in the region.

Southern-Eastern Europe

Owing to the diversity of transition gaps and opportunities and the Bank's deep engagement in Southern-Eastern Europe, the distribution of strategy priorities is broad, with commitments under the competitive, resilient, well-governed, integrated and green qualities across the region.[6] Policy priority objectives focus particularly on development of more competitive and green economies.

To make the region more **competitive**, the Bank seeks to promote a more dynamic private sector through (i) increasing operational efficiency, promoting skills and technology transfer, and supporting and scaling up the SME sector specifically; and (ii) promoting privatisation and commercialisation efforts with an emphasis on infrastructure and municipal services. This aligns with the Bank's efforts to advance **good governance** by focusing on better corporate governance and improving the investment climate through engagement in investment councils.

Under **resilience**, the Bank targets both the financial and energy sectors. In Romania and Bulgaria, the Bank prioritises financial resilience through diversifying sources of finance, market consolidation, resolving the burden of NPLs and deepening financial intermediation in under-served regions. Similarly, in Serbia efforts aim at developing non-banking financial institutions and local currency lending. In more fragile markets, the Bank focuses on supporting access to finance to restart bank lending altogether (Albania) and decrease Euro-isation (Macedonia). Ensuring energy security is a priority particularly in Albania (in collaboration with other IFIs) and Kosovo.

Integration is an important priority in the Western Balkans, covering both physical infrastructure (regional connectivity in energy and transport) and support for trade and investment flows through trade finance credit lines, accompanied by small business advice on exports and co-ordinated policy dialogue.

To promote a **greener** region**,** increasing energy efficiency is a theme across a majority of countries. Objectives include increasing the share of renewable resources, lending for energy efficiency in the public sector and improving the quality of the environment (waste water treatment plants, non-polluting public transport).

[5] The first country strategy for Tunisia is scheduled for the third quarter of 2018.

[6] As country strategies for Serbia and Macedonia are due for revision in the first part of 2018, a more consolidated approach to the region is expected in coming years.

Box 4: Implementing the Strategy for the Promotion of Gender Equality

The Bank's first Strategy for the Promotion of Gender Equality (SPGE) was approved in 2015 and is an instrument for delivering the SCF objective of mainstreaming gender and inclusion. External delivery and outcomes of the Bank's work in this area is tracked through Country Strategy results frameworks. Operational objectives are captured in the transition section of the Corporate Scorecard and cascaded via Departmental scorecards throughout the Bank. Both operational objectives and the objective of strengthening the institutional capacity for gender mainstreaming is reported through the Quarterly Performance Report as of the third quarter of 2017, based on the indicators set out in the SPGE's Monitoring Framework. Some highlights of the Bank's extensive work in this area are:

- Awareness of gender issues in the Bank has substantially increased and staff capacity to address gender issues in their work strengthened through training on strategy implementation with six sector teams; 12 country offices, the Evaluation Department, and the Procurement Department to date. Gender has been incorporated into a number of operational and business tools.
- Appointments with a gender focus include: a Gender Focal Point for Central Asia based in the Bishkek RO, a Gender Programme Coordinator for the Refugee Response in Turkey based in the Ankara RO, and two bankers with gender coordination functions in the ROs in Morocco and Egypt.
- Further progress made in mainstreaming gender in the Bank's climate change and energy efficiency work. Funding for gender work was a key part of the Bank's funding proposal to the Green Climate Fund for Green Energy Financing Facilities (GEFF) in 10 countries of operations. Other projects supported by the GCF have also included gender components in SEMED and Central Asia.
- All Bank projects have been screened for gender impact since 2014. Gender issues are identified as part of Private Sector Diagnostics and addressed in all Country Strategies.
- By end September 2017, 21 gender projects have been signed, a 25 per cent increase on the same period in 2016. Of these, seven addressed Access to employment and skills; eleven Access to finance; and three Access to services. The total number of projects with a gender component is 105;
- Knowledge management products have been produced and disseminated, including toolkits for safer transport, district heating, and gender responsive investment climate.
- A range of TC assignments have been undertaken with donor and SSF support, including actions to support gender equality in the Bank's refugee response and a TC framework has been established to support the provision of gender advisory services;
- Priority Policy Objectives with gender components have been established in Kazakhstan, Turkey and Jordan. Stand-alone policy engagements to support governments in improving the enabling environment for women's economic inclusion and gender equality have been undertaken, for example, the governments of both Kazakhstan the Kyrgyz Republic requested the Bank to submit recommendations and priorities to ongoing official reviews of professions banned for women.
- The Bank has collaborated strongly with a range of other institutions and in addition chaired the MDB Working Group on Gender until June 2017;
- Data provision for formulating country and project level indicators has been strengthened. Gender is fully integrated in the revised transition methodology and its operationalisation.

Turkey

In Turkey, the Bank pursues wide-ranging transition objectives. Support for a more **competitive** economy through improving the quality of municipal services and fostering innovation and efficiency in the corporate sector, for example, through investment in venture capital. Under **good governance**, the focus is on improving corporate governance practices and business operating standards through investments (including private equity) and business advisory services.

The Bank promotes increasing private sector participation in the power and natural resource sector, thus strengthening **resilience** in the energy sector; while financial resilience objectives include advancing of financial product diversification via supporting development of stock exchanges and broadening the range of capital market products.

Inclusion is a central priority, with work to increase economic opportunities for women and youth both via investment (including the Women in Business programme) and policy dialogue. Serving the needs of refugees through training and the SME sector is a further policy dialogue priority. The Bank also focuses on the **green** economy by supporting reduction in energy intensity across sectors and improvement in the institutional environment for energy efficiency (including its engagement in the National Renewable Energy Action Plan).

4.2 Transition and the Corporate Scorecard

The 2017 Corporate Scorecard contained objectives for average Expected and Portfolio Transition Impact (ETI, PTI) and progress under each of the six qualities of the revised transition concept using a Composite Performance Assessment (CPA).

The minimum level of ETI and PTI in the scorecard remains at 60 and 65, respectively, for 2018. The structure of the CPAs remains as in 2017, with the choice of qualitative and quantitative indicators for each quality aiming to achieve balanced coverage across the whole transition dimension while avoiding a burdensome or confusing proliferation of metrics.

The specific **reporting indicators** for each quality remain also largely as in 2017:

- **Competitive, innovative economies:** a hard floor of 75 per cent for successful implementation of operations (both investments and policy engagements) targeting this transition quality; tracking indicators capturing the number of: projects with a Competitive objective; loans to SMEs financed through intermediaries and the impact of ASB operations on SMEs' turnover; and an account of qualitative achievements.
- **Well-governed economies and firms:** a hard floor of 75 per cent for successful implementation of operations (both investments and policy engagements) targeting this transition quality; tracking indicators capturing the number of operations with a Well-Governed objective; the number of Comprehensive Governance Action Plans (CGAPs) agreed with clients; and an account of qualitative achievements.
- **Environmentally sustainable, green economies:** a hard floor of 75 per cent for successful implementation of operations (both investments and policy engagements) targeting this transition quality. The Bank has set a strategic objective to reach a ratio of GET financing of 40 percent by 2020 and will endeavour to deliver this as soon as possiblewhile making progress towards the target from year to year. For planning purposes in 2018, a GET ABI ratio of 36 per cent based on the mid-point of the proposed business plan is set. Further measures are: tracking indicators capturing the number of operations with climate adaptation, water and/or waste minimisation components; estimated annual CO_2 emissions reduction and the number of sub-loans financed by GEFFs (formerly SEFFs); and qualitative achievements focusing on policy dialogue and advisory work.
- **Gender-equal, inclusive economies:** a hard floor of 75 per cent for successful implementation of operations (both investments and policy engagements) targeting this transition quality; tracking indicators capturing the number of: new investments with either a gender component or focus; MSME sub-loans under Women in Business programmes; ASB operations with women-owned companies; operations with an Inclusive objective; new investments with a youth or regional inclusion focus or component and an account of qualitative achievements.
- **Resilient economies and firms** a hard floor of 75 per cent for successful implementation of operations (both investments and policy engagements) targeting this transition quality; tracking indicators capturing the number of: operations with a Resilient objective; transactions contributing to local capital market development; the proportion of debt investments in local currency and the net changes in the capital adequacy ratio of partner banks and an account of qualitative achievements.
- **Well-integrated, connected markets:** a hard floor of 75 per cent for successful implementation of operations (both investments and engagements) targeting this transition

quality; a tracking indicator capturing the number of: projects with an Integration objective and TFP transactions supported by partner banks; and a qualitative account of results focusing on policy dialogue and advisory work.

As in 2017, the CPA process will be conducted as follows:

- Each quantitative indicator will be assessed against its floor (where it exists) or against a three year rolling average, as 'strong', 'fair' or 'weak'.
- Qualitative indicators will be assessed as 'strong', 'fair', or 'weak' based on the magnitude and scope of results achieved in the year taking account of defined objectives and transition and operational factors.

The overall CPA of Very Good, Good or Needs Attention will be derived by combining the assessments above.

5. BANK ACTIVITY

Section 4 provided an overview of the Bank's transition objectives and a high level account of the instruments that would be used to further those objectives. This section focuses on the Bank's level and distribution of investment activities in pursuit of those objectives. These quantifiable activities will – as section 4.1 implies – be complemented by policy work. Accordingly this section is structured as follows:

- Section 5.1 shows how the Bank's strategic directions set out in the SCF are combined with the analysis of transition delivery, financial returns and transition opportunity to produce a portfolio which balances the Bank's objectives;
- Section 5.2 presents a projection of the Bank's investment activity over the three years covered by the SIP, the underlying assumptions together with objectives for 2018; and
- Section 5.3 gives a picture of the evolution of the Bank's grant use over the period covered by the SIP.

5.1 Strategic Foundations

The analysis presented in this section underpins the Bank's Strategic Portfolio Management approach and aims to inform the direction of the Bank's activities from 2018 to 2020, considering three factors:

- Strategic directions of the SCF, described in box 1, presented in the Introduction;
- The business environment, including the evolution of the Bank's pipeline;
- An analysis of trends in transition impact, financial returns and risks in the portfolio.

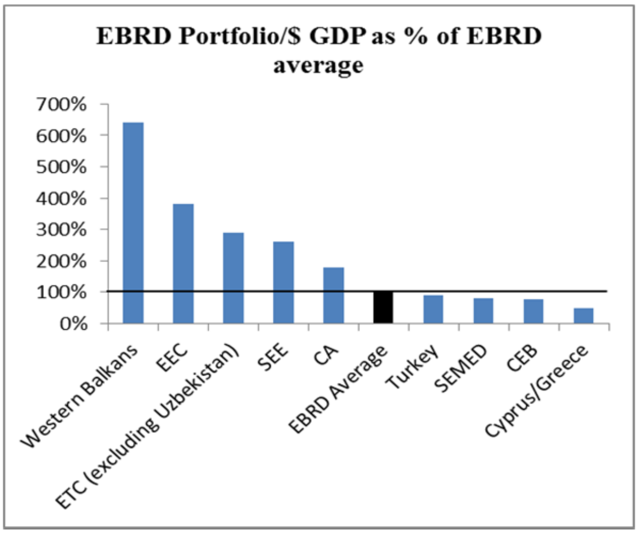
The results of this analysis cannot be applied mechanically, but inform the process by which the operational plan is developed.

5.1.1 Regional directions

The SCF directs the Bank to focus its engagement on countries less advanced in transition – in particular, the ETCs, Western Balkans and SEMED countries. Chart 5.1 gives an overview of the intensity of EBRD activity across its regions of operations.

It provides a snapshot of the Bank's portfolio at end 2016, expressed in terms of the ratio of portfolio amount to GDP size, and standardised to the Bank's average across all countries of operations. The regions on the left side of the chart all show a high intensity of activity, relative to the EBRD average level (normalised at 100 per cent and shown by the horizontal line).

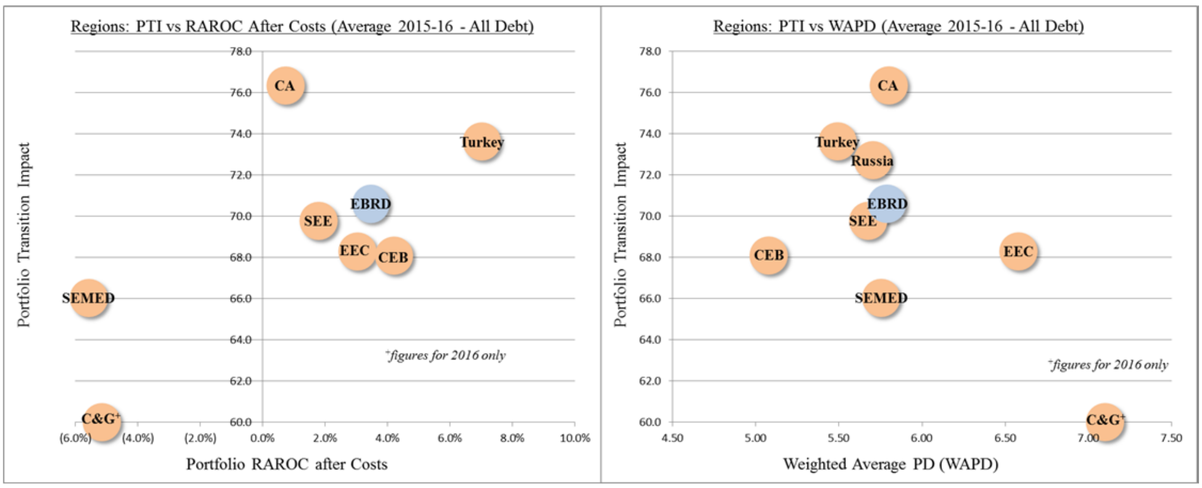
Chart 5.1: Relative Regional Intensity of Portfolio by Region



The chart shows that the Bank continues to be well placed to deliver on the SCF directions to emphasise ‘countries and regions within countries that are less advanced in transition’, with the Western Balkans showing the greatest relative intensity. The portfolio intensity in SEMED also grew significantly in 2016, from 63 per cent of the Bank average in 2015 to the current level of 81 per cent, showing the continuing ramp-up of activity in a relatively new region for the Bank, although this remains below the level for regions containing countries at a similar level of transition. Consistent with market developments and the Bank’s strategic goals, including the approach to graduation as set out in the SCF, the intensity of lending in more advanced transition countries is lower. Looking forward, as stated in the SCF ‘as the transition becomes still more advanced, the level of activity of the Bank in a country will decrease as a consequence of the fewer market segments in which Bank investments can satisfy its operating principles (transition impact, sound banking and additionality)’.

Regional analysis of transition impact, financial returns and risks across the portfolio gives an empirical basis for understanding the implications of operational planning decisions, the interplay among the Bank’s various goals, and the balance of the portfolio. The analysis in chart 5.2 below is based on both non-sovereign and sovereign debt – covering over 80 per cent of the whole portfolio – averaged over two years (2015-16) to increase the stability in the data, and including the allocation of full costs.

Chart 5.2: Regional Portfolio Transition Impact by Return and Risk



Consistent with the theme of this SIP, the results are broadly similar to last year. Central Asia remains the strongest region for transition impact, with relatively weak RAROC, reflecting the small average size of projects and high costs of doing business. Turkey stands out for its strong performance on both transition impact and RAROC. SEMED, on the other hand, lags on both indicators; although trends in projects signed since October 2016 suggest some improvement. The Cyprus and Greece portfolios are still immature and the negative RAROC is a reflection of the costs of ramping up activities. The greatest average risk is seen in Cyprus and Greece and the EEC region, while the CEB region presents the lowest risks – largely reflecting the sovereign risk ratings in those two regions.

By its nature, the data is retrospective and relies on underlying assumptions about costs, expected losses and provisions. However, taken in conjunction with the observations on strategy and demand, as well as with risk concentration considerations, these provide a meaningful foundation for decision making.

Looking ahead, the pipeline stock per region provides a useful indication of the level of investment opportunities across the Bank's regions. Viable and robust pipelines are key to the Bank's ability to realise its operational strategy. Pipeline evolution reflects many factors, but at August 2017, relatively strong pipeline stock compared to 2016 levels is seen in Cyprus and Greece – where engagement is time-bound and frontloaded – together with SEE and EEC, consistent with the strategic objectives of the SCF.

Drawing together the analysis, pipeline, and strategic directions, the SIP 2018-2020 assumes the following changes relative to the SIP 2017-19 geographic directions:

- A slight increase in Eastern Europe and the Caucasus, assuming a gradual increase in activity in Ukraine after a period of decreased ABI;
- A slight increase in SEMED reflecting the strategic emphasis on the region in the SCF, and the increased opportunities presented by recent accessions; and
- No significant changes in Central Asia, Central Europe and Baltics, Cyprus and Greece, South Eastern Europe or Turkey.

5.1.2 Sectoral and product directions

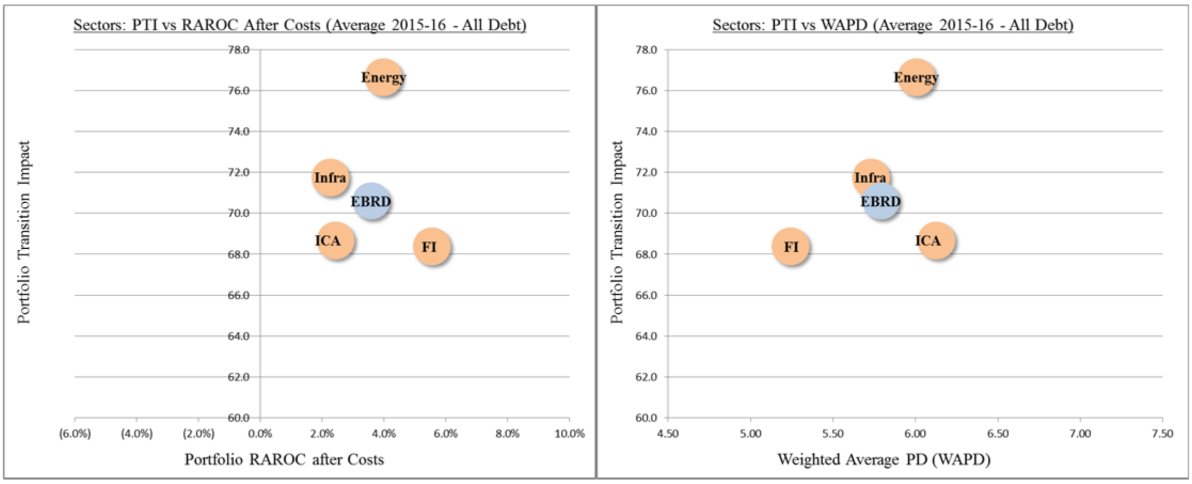
The SCF provides less comprehensive direction on sectoral priorities. Also, the SPM analysis for sectors shows less dispersion than that observed across regions. The performance of the sectors across the dimensions analysed is fairly clustered.

Chart 5.3 sets out the sectoral analysis of transition impact, financial returns and risks across the non-sovereign and sovereign debt portfolio on the same basis described in the previous section.

Once again, the picture is broadly similar to last year, with Energy the strongest on transition impact and Financial Institutions leading on financial returns (although there has been a notable downward trend in margins in some regions for Financial Institutions projects signed since late 2016.) Transition impact on deals in the Corporate sector, which was noted as a concern in the SIP2017-19, has improved significantly. The Corporate sector also continues to be marginally the riskiest, while Financial Institutions present the lowest average risk.

Comparison of the pipeline stock levels between August 2017 and 2016 shows slightly increased opportunities in the Financial Institutions sector, while the Energy sector has weakened.

Chart 5.3: Sectoral Portfolio Transition Impact by Return and Risk



Drawing on all these factors, the SIP2018-20 assesses the following marginal changes relative to the SIP2017-19 sectoral directions:

- A decrease in the **energy sector** driven primarily by a trend towards smaller project sizes as (for example) green energy increasingly takes the place of larger traditional utility projects;
- An increase in the **financial sector** reflecting a strong pipeline and good financial performance;
- A relatively flat profile for the **corporate sector** reflecting a balance between its strategic importance from a private sector development perspective and a downward pressure on average project size; and
- A decrease in the **infrastructure sector** relative to previous expectations driven by a lower number of large transport transactions and an increase in the number of small transactions in municipal infrastructure.

Equity Investments

Investing in equity is a fundamentally different business from debt financing. Consequently, it requires a different approach to strategic analysis and planning. Amongst the most important differences are:

- Far greater cyclical variation and underlying volatility, so historic trends in equity returns are a poor guide to future performance;
- An emphasis on quality rather than volume due to the inherent risk; and
- Labour intensity, with the ratio of deals pursued to deals closed is an order of magnitude greater.

The Bank has a set of guidelines that drive equity selection and set the desired risk/reward characteristics for new investments. Geographically, the approach is necessarily opportunistic and focused on quality (both transition and financial) rather than volume. In general, opportunities tend to be more numerous in larger, and more advanced, transition countries. As the Bank's region lags behind other regions in the size and scope of its equity markets, it remains challenging to find opportunities which meet the Bank's requirements. Over-liquid financial markets mean that debt finance is more financially attractive for firms which might otherwise be seeking equity investment. This is particularly the case for mid-sized companies, a group which the Bank sees as most promising for yielding superior returns. Equally, private equity fundraising in the Bank's region as a percentage of GDP is well below that seen in other regions. Although interest seems to be strengthening, this still restricts the number of co-investment opportunities – either directly or through investment in Funds – to take advantage of. The result has been a historically low share of equity investment in 2017 (at around 5% of ABI). Therefore it is unlikely that the SCF aspiration to increase the share of equity investments in the Bank's portfolio will be met during the period of this SIP. For planning purposes an equity share of 10% in ABI is assumed, although this is neither a target nor a cap.

5.2 Investment activity

This section presents an assessment of the projected evolution of the Bank's investment portfolio over the period 2017 to 2020 in line with its strategic objectives and operating principles. This assessment takes account of consultations with the Board of Directors and of the strategic planning process underpinning the SIP including views from sector and country banking groups about the transition business opportunities over the period considered.

Annual Activity 2017-2020

Uncertainty related to the operational environment in several large countries of operations is expected to continue into and beyond 2018. With over half of the Bank's annual investment concentrated in the five largest countries of operations and downward pressure in the average size of the Bank's projects, the likelihood of achieving investment levels at the upper end of the range simultaneously across all major countries of operations is limited. In spite of this uncertain context, and reflecting an ambitious approach, the upper end of the ABI range for 2018 is proposed to be maintained at €9.0 billion, equal to the level indicated in the SIP 2017-2019. Consistent with this approach, a marginal increase of the upper end of the ABI range to €9.1 billion is proposed for 2019 and 2020.

Overall, the geographical distribution of annual activity levels is projected to be broadly consistent with the Bank's strategic directions underpinned by the following assumptions:

- Equity share of ABI is projected at up to 10%, based on the latest trends and an assessment of current pipeline;
- Sovereign lending is projected at around 18% of ABI reflecting activity in the energy and infrastructure sectors and in line with current trends and SIP 2017-2019 projection;
- Under the current guidance of Directors, Management may conduct selective defensive portfolio and restructuring operations in Russia. Based on portfolio dynamics over the past two years and the marginal amount of restructuring operations conducted in the country over the previous period, no ABI is currently assumed in the SIP 2018-2020 in Russia; and
- Reflecting recent activity trends, trade facilitation is projected at around 10% of Annual Bank Investment, similar to the level observed in 2016 and in the first eight months of 2017. This compares with an historical average of 8% over the period 2012 to 2015.

Table 5.1: Number of operations and Annual Bank Investment 2016-2020

	2016	**2017**	**2018**	**2019**	**2020**
€ billion at planning rate €/$1.15	**Act.**	**Est.**	**Proj.**	**Proj.**	**Proj.**
Annual Bank Investment	9.0	8.7*	9.0	9.1	9.1
Number of Operations	378	360-400	360-400	370-410	370-410

* 2017 ABI is estimated in a range of €8.5 to €8.9 billion with a mid-point at 8.7 billion based on signings to date and current pipeline trends.

At end August 2017, the number of projects signed was 192 equivalent to the number signed at end August 2016. The number of operations for the SIP period is projected as a range with the lower end similar to the SIP 2017-2019 and a lower upper end reflecting a growing share of trade facilitation in ABI Table 5.1 above shows the projected ABI and number of operations for the SIP period 2018 to 2020.

Portfolio and Operating Assets Development

Annual disbursements in 2016 were largely influenced by the significantly back loaded activity in 2015. As a result, 2016 disbursement reached €7.5 billion with disbursements in the first half of 2016 including €1.3 billion of disbursements from projects signed in the second half of 2015, double the amount for the same period in 2015. Disbursement activity in the first eight months of 2017 shows a pattern closer to more experience prior to 2015 with around €4.0 billion disbursed at the end of August 2017, below end August 2016 level (€4.8 billion) but well above end August 2015 (€3.2 billion). Reflecting these trends and the stable projected level of activity for the period, annual disbursements are projected to remain around €6.7 billion for the planning period.

Table 5.2: Annual disbursements 2016-2020

	2016	**2017**	**2018**	**2019**	**2020**
€ billion at planning rate €/$1.15	**Act.**	**Est.**	**Proj.**	**Proj.**	**Proj.**
Disbursements	7.5	6.7	6.7	6.7	6.8

Reflow projections are based on an analysis of individual reflow parameters which are either estimated on the basis of actual information (this is the case for scheduled repayments on existing operating assets) or of ratios to operating assets (for prepayments, divestments, and write-offs) or portfolio (cancellations). Projections for main reflow parameters for the SIP period are based on the following assumptions:

- Future repayment projections are established on the basis of scheduled repayments for existing operating assets and repayment profiles for new commitments based on historical trend analysis, taking into consideration the projected level of loan impairment. Annual repayments are projected at around 18% of the unimpaired loan operating asset stock similar to the historical average for the period 2014 to 2016 and to the projected SIP 2017-2019 level.
- Annual prepayments rose sharply in 2016 reflecting a number of large prepayments on projects in Ukraine and the Russian Federation. As a result, the level of annual prepayment increased from 3% of unimpaired loan operating assets in 2015 to 10% in 2016. The trend in the first eight months of 2017 shows a slowing in the volume of prepayment to around half of the end August 2016 level. As a result, prepayments are projected at around 6% of unimpaired loan operating assets for the SIP period 2018 to 2020, above the projected level of 5% in the SIP 2017-2019.
- Annual divestments reached €0.7 billion in the first eight months of 2017, similar to the 2016 full year result reflecting strong divestments trends in South Eastern Europe and Central Europe. Based on an examination of the stock of the Bank's current investments and possible exit opportunities, divestments are expected to reach around 18% of equity operating assets in 2017 and are projected at around 14% for the period 2017 to 2020, above the rate of 12% in the SIP 2017-2019. In volume terms, divestments are projected at around €2.3 billion for the period 2018 to 2020.
- Cancellation rates in Central Europe, South-Eastern Europe and SEMED, with cancellation volume reaching €1.0 billion in the first eight months of the year compared to an average of €0.7 billion for the same period in 2014-2016. Reflecting recent trends, annual cancellations are projected at around 10% of undrawn commitments for the SIP 2018-2020, up from 8% in the SIP 2017-2019.

Table 5.3: Portfolio reflows 2016-2020

	2016	2017	2018	2019	2020
€ billion at planning rate €/$1.15	**Act.**	**Est.**	**Proj.**	**Proj.**	**Proj.**
Portfolio Reflows	7.8	7.9	7.3	7.0	7.2

As a result of the above assumptions, annual reflows are projected at around 19% of total portfolio in 2017 and to remain at around 17% for the period 2018 to 2020.

Building the Bank's operating assets is a constant focus. Table 5.4 provides medium term projections of portfolio and operating assets levels across the Bank's region of operations resulting from the above annual activity, disbursement and reflow projections. These operational projections form the basis of the financial and capital utilisation projections developed later in this document. Notable features of the portfolio are that:

- It is projected to increase by 7% from €40.6 billion at the end of 2016 to €43.6 billion at the end of 2020. Operating assets are projected to grow by the same percentage from €28.9 billion at the end of 2016 to €30.7 billion by the end of 2020.
- In countries other than the Russian Federation is projected to grow by around 16% in the period 2016 to 2020 from €36.6 billion to €42.3 billion; and
- Taking into account the projected portfolio growth and historic trends of the average project size and continuing reflow pressure, the number of active projects in the Bank portfolio is projected to grow from 1,853 at the end of 2016 to between 1,900 and 2,100 operations by the end of 2020, an increase in a range of 3% to 13% depending on average project size.

Table 5.4: Portfolio and operating assets 2016-2020

	2016	2017	2018	2019	2020
€ billion at planning rate €/$1.15	**Act.**	**Est.**	**Proj.**	**Proj.**	**Proj.**
Portfolio	40.6	40.7	41.5	42.7	43.6
Operating Assets	28.9	29.2	29.6	30.2	30.7
Active Portfolio Operations	1,853	1850-1950	1870-2070	1880-2080	1900-2100

Table 5.5 provides an illustrative projection of the Bank's portfolio regional composition to 2020. This distribution reflects the directions set out in the SCF and the continuing implementation of the SPM approach, as well as the transition business opportunities anticipated over the period. It is also reflective of the different activity levels, product composition and reflow rates across the regions of the Bank as well as of the maturity of the portfolio in each region – the areas of more rapid build-up of portfolio tend to be those where the Bank's work is less mature and reflow rates lower.

Reflecting the above planning parameters, an examination of the portfolio projections for the SIP covering the period 2018 to 2020 shows that:

- By the end of the period in 2020, the three largest regional portfolios are projected to be Eastern Europe and Caucasus (€7.4 billion), South Eastern Europe (€7.8 billion) and Turkey (€8.2 billion).

Table 5.5: Illustrative regional portfolio composition 2016-2020

	2016	2017	2018	2019	2020

€ billion at planning rate €/$1.15	Act.	Est.	Proj.	Proj.	Proj.
Central Asia	4.1	4.4	4.5	4.6	4.5
Central Europe and Baltics	6.1	5.9	5.7	5.6	5.7
Cyprus and Greece	0.9	1.3	1.6	1.9	2.0
Eastern Europe and Caucasus	7.1	6.8	6.9	7.2	7.4
Russia	4.0	3.0	2.2	1.7	1.3
South-Eastern Europe	7.8	7.8	7.8	7.8	7.8
Southern and Eastern Mediterranean	3.7	4.4	5.2	6.0	6.7
Turkey	6.8	7.1	7.6	7.9	8.2
Total	**40.6**	**40.7**	**41.5**	**42.7**	**43.6**

	2016	2017	2018	2019	2020
% Share	Act.	Est.	Proj.	Proj.	Proj.
Central Asia	10%	11%	11%	11%	10%
Central Europe and Baltics	15%	15%	14%	13%	13%
Cyprus and Greece	2%	3%	4%	4%	5%
Eastern Europe and Caucasus	18%	17%	17%	17%	17%
Russia	10%	7%	5%	4%	3%
South-Eastern Europe	19%	19%	19%	18%	18%
Southern and Eastern Mediterranean	9%	11%	13%	14%	15%
Turkey	17%	18%	18%	18%	19%

- The Central Asia portfolio is projected to grow by 9% from €4.1 billion at end 2016 to €4.5 billion at end 2020.
- The Central Europe and Baltics portfolio is projected to decrease marginally from €5.9 billion at end 2017 to €5.7 billion at end 2020, reflecting a relatively high projected reflow level over the SIP period as a result of strong divestment and cancellation trends.
- The portfolio in Cyprus and Greece is projected to grow from €0.9 billion to €2.0 billion at end 2020 with a growing reflow rate over the period reflecting the rising maturity of the region's portfolio.
- The Russia portfolio trend reflects portfolio dynamics to date including high prepayments and a likely increase in divestments given the evolving product composition of the portfolio.
- The portfolio in South Eastern Europe is projected to remain broadly constant at around €7.8 billion reflecting the advanced maturity of the Bank's assets in the region and a constant flow of new projects over the SIP period.
- The portfolio in Turkey is projected to reach €8.2 billion.
- A determined effort will be made to contain portfolio growth through active mobilisation of external financing to reduce EBRD exposure and, where possible, through selective portfolio sale.
- The SEMED portfolio is projected to increase by 81% and reach €6.7 billion at end of 2020, reflecting new activity levels and a relatively low projected reflow level of €2.8 billion over the next four years.

5.2.1 2018 Scorecard Parameters

Based on the above projections, the following operational performance ranges are proposed for 2018 to deliver the strategic objectives of the EBRD:

- **Number of operations** range of **360 to 400** reflecting the ABI range and average project size dynamics**.**
- **ABI** range of **€8.1 to €9.0 billion** reflecting current pipeline trends, strategic approach and business development activity.
- To promote the mobilisation[7] of external finance on the Bank's projects the **fungibility** between EBRD finance (ABI) and Annual Mobilised Investment (AMI) is maintained at **€0.7 billion** in 2018 while keeping an **Annual Mobilised Investment (AMI)** floor of **€0.8 billion**.
- A combined ABI and AMI floor of **€8.9 billion** to maintain the EBRD operating assets base and revenue generating capacity. Allowing for €0.7 billion of fungibility between EBRD and mobilised external finance results in an ABI range of €7.3 billion to €9.0 billion, with the lower end of the range assuming the maximum fungibility of €0.7 billion.
- **Annual disbursement** range of **€5.4 billion to €6.7 billion** in line with the ABI range for 2018 with the lower end reflecting the potential impact of ABI/AMI fungibility.

These objectives do not constrain the Bank's ambition. Consistent with the aim of increasing the Bank's operating assets, should the business and transition environment prove more favourable leading to the identification of more opportunities, including for Green, equity and mobilisied investment, it may be possible to exceed these objectives.

An indicative geographic and sector composition of annual Bank investment for 2018 is shown in table 5.6.

Table 5.6: 2018 Indicative regional and sectoral Annual Bank Investment

	2017 BP	2018 BP

[7] The Bank uses a strict definition of AMI for the scorecard which is limited to 'the volume of commitments from entities other than the Bank made available to the client due to EBRD's direct involvement in mobilising external financing'. This definition is in line with the definition of mobilisation recently agreed amongst MDBs and set out in *Mobilization of Private Finance by Multilateral Development Banks – 2016 Joint Report*. In addition to direct mobilisation, the Bank also measures the amount of external finance provided by other sources such as other MDBs, private corporates and banks, institutional investors and public budgets at national or local level. External finance linked to EBRD signed operations during 2016 totalled €17.4 billion.

€ billion at planning rate €/$1.15	Indicative Share	Indicative Share	Indicative mid -point ABI
Central Asia	11%	11%	900
Central Europe and Baltics	15%	14%	1,200
Cyprus and Greece	7%	7%	600
Eastern Europe and Caucasus	15%	17%	1,450
South-Eastern Europe	16%	16%	1,350
Southern and Eastern Mediterranean	16%	18%	1,500
Turkey	19%	18%	1,500

* The 2017 BP also included up to €100 million for selected defensive portfolio and restructuring operations in the Russian Federation.

	2017 BP	**2018 BP**	
€ billion at planning rate €/$1.15	**Indicative Share**	**Indicative Share**	**Indicative mid -point ABI**
Corporate	26%	25%	2,100
Financial Institutions	27%	28%	2,400
Energy	23%	24%	2,000
Infrastructure	24%	24%	2,000

5.3 Grant and concessional finance and donors

In order to support its activities to deliver the objectives outlined in the previous sections, the Bank mobilises funds from its donors as well its net income. In general, donor funds are used to address affordability constraints, improve market outcomes in the presence of significant externalities and increase the sustainability and transition impact of its work. The growth of these resources over time has been led by the development of the Bank's strategic objectives, particularly in the less advanced parts of the Bank's region. Given the Bank's private sector mandate and business model, grants are used selectively, and only where they do not create situations of dependency or distort markets.

Donor funds can comprise either non-reimbursable grants or reimbursable instruments, such as concessional loans. Non-reimbursable grants cover both technical cooperation grants (for example, assistance in project preparation and implementation or policy dialogue) or co-investment grants (for example, capital expenditure grants for investments, risk-sharing facilities, guarantees, incentives).

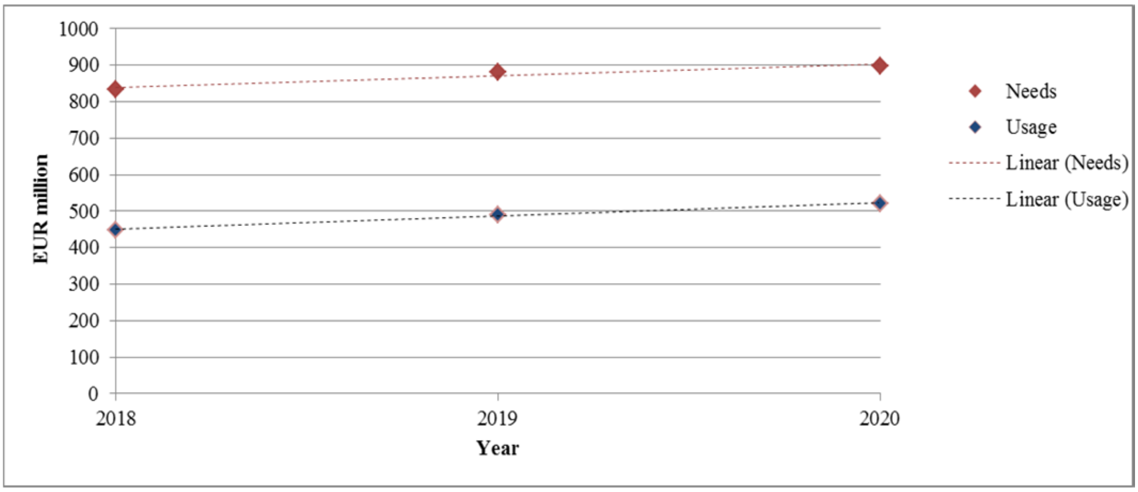
This section looks at estimated needs of such funds over the period covered by this SIP, derived from a bottom up exercise across the Banks' operational departments. Based on this exercise the Bank determines indicative fundraising targets for the same period.

The Bank has a good track record. In the latest full year the overall fundraising target – covering both grants and concessional finance – of €400 million was exceeded by more than 10%. In doing this, the Bank has been aiming to widen its donor base, actively engaging with a range of new donors, including the private sector, philanthropic organisations, countries of operations and multilateral donors, notably the Green Climate Fund. In addition, the Bank has been deepening its relationship with the EU. These are all ongoing efforts.

5.3.1 Projection of funding need 2018 - 2020

Chart 5.4 shows the preliminary funding needs and usage of grants projection for 2018-2020.

Chart 5.4: Grant needs and usage[8] 2018- 2020



This estimation is indicative, as some of the pipeline projects are at an exploratory stage and may not materialise, change or may be delayed.

5.3.2 Analysis of 2018 funding needs and gaps

Total **grant funding needs** have been identified for 2018 amounting to €833 million, which is about 20% greater than in previous years and reflect the growing importance of grants for the Bank's activities. Across all of EBRD's regions grant needs remain the highest for green transition, with 47% of total funding needs. Around 10% of all operational funding needs relate to non-transactional grants including for capacity building and policy engagement initiatives. From a geographic perspective ETC and SEMED remain the regions with the greatest funding needs, as they have the highest affordability constraints and a strong need for energy efficiency improvements. Funding needs in these two regions are further intensified by the Bank's re-engagement in Uzbekistan and setting up of operations in Lebanon and West Bank and Gaza.

Taking into account the stock of funds available for new projects leaves a funding gap of €759 million.

5.3.3 Fundraising and strategy

Based on this analysis and the Bank's planned activities, indicative fundraising targets for grants and concessional finance are established for the period covered by the SIP. These targets also take into account a realistic assessment of likely grant funds availability; particularly as traditional donor funds for the Bank are increasingly scarce.

In line with plans outlined in the previous SIP 2017-2019, the Bank has started a more programmatic approach towards **concessional finance.** In doing so, the Bank has secured €529 million in concessional funding from the Green Climate Fund in 2017, which greatly exceeds the original fundraising target for concessional finance set in the SIP 2017-2019 (€158 million per year). The Bank estimates its needs for concessional finance to amount to €95 million for 2018. Given the important inflows of new concessional funds for climate finance in recent time and the build-up of the current GCF-funded climate portfolio, funding needs for concessional finance is likely to be significantly lower in future years.

[8] Excluding funding related to concessional finance and refugee response

Chart 5.4: Funding needs vs. Fundraising targets

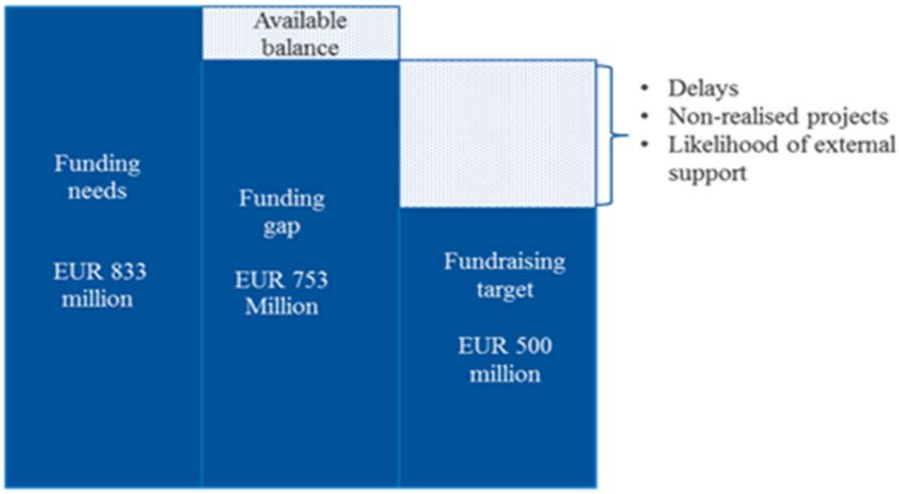


Table 5.7 shows a summary of indicative targets for 2018-2020 for both grants and concessional finance.

Table 5.7: Indicative fundraising targets 2018-2020

Sources	2018 (target)	2019 (target)	2020 (target)
Donor inflows	400	425	432
SSF	100	100	100
Total target	**500**	**515**	**525**
Concessional finance	95	100	105

The fundraising targets remain ambitious. They take account of both the Bank's ability and likelihood to successfully mobilise important fund levels on an annual basis, and an increasingly challenging donor landscape where competition for resources is fierce. Moreover, they reflect the anticipated translation of planned funding needs into concrete project pipelines in a given year. The Bank will aim to raise these funds focussing on the following priorities:

- **Continued move towards more programmatic funding** to support efficiency, predictability, impact, scale and leverage. In 2018, the focus is to implement and continue to raise funds for the Green Economy Transition (including strategic dialogue ahead of GEF-7 and continuing to build the relationship with the GCF), securing access to the new EU External Investment Programme (EIP) and replenishing the EBRD multi-donor funds.
- **In-country and regional engagement** to access donor resources available at country level and foster coordination between the Bank, the IFIs and the broader donor/international organisation community. This will mean particularly engaging closely with: EU delegations; countries of operations that are also EU member states to draw on structural and cohesion funds and bilateral donors.
- **Broadening the donor base** to create a more diversified set of donor partnerships and engage in innovative approaches. For 2018, priorities are: to encourage more countries of operations to establish donor funds; pro-actively engage with new potential partners such as the Gulf Cooperation Council and related donors, China, new multilateral facilities as

well as philanthropic foundations and the private sector and finding new ways of working with the EU and other existing donors to identify.

- **Focus areas for 2018** include efforts to mobilise support for the Bank's relatively new priorities including: policy engagement; operations in the West Bank and Gaza, Lebanon and Uzbekistan and the Refugee Response Programme.

SECURING FINANCIAL SUSTAINABILITY

6. FINANCE AND CAPITAL

Financial sustainability is essential to the Bank's continuing ability to deliver its transition mission. The key conclusion of this section is that **the Bank has sufficient capital capacity now and in the future to both support and implement its strategy in the period of this SIP and to withstand potential losses from stress events**. The Bank is projected to remain comfortably in conformity with the capital control parameters set out in the Strategic and Capital Framework and retains some capital headroom to support additional operational activity to deliver shareholders' objectives in the Bank's countries of operations.

The structure of the section is:

- Section 6.1 reviews improvements in the Bank's framework to **appropriately balance financial and transition objectives**;
- Section 6.2 presents **medium term projections of**: overall growth in capital, the potential for net income allocations and capital utilisation;
- Section 6.3 assesses **the financial resilience of the plan**, including the potential impact of stress events;
- Section 6.4 sets out the **2018 financial objectives**; and
- Section 6.5 details the level of **the 2018 Borrowing Programme** necessary to achieve a prudent level of liquidity by the end of 2018.

6.1 Financial sustainability

Securing the Bank's **financial sustainability** over the medium term whilst fulfilling its transition mandate is captured through the overall objectives to:

- Sustainably grow capital to support transition and operational objectives, provide a buffer against shock events and to allow for net income allocations to support the Bank's operational priorities; and
- Maintain prudent levels of capitalisation and liquidity and demonstrate sound financial management to support the Bank's triple-A credit rating.

In order to support the delivery of these objectives, the Bank has developed tools, policies and approaches over recent years that together form a coherent system for assessing, monitoring and influencing the factors which impact on long term financial sustainability**.** The components of this system are:

- **Prudent capital policies** – the Statutory Capital Policy and the Capital Adequacy Policy – to ensure appropriate capitalisation levels to withstand unexpected losses and support the triple-A rating;
- An appropriate **Provisioning Policy** which ensures adequate coverage of expected losses;
- A reinforced **Liquidity Policy,** incorporating stress scenarios for the sizing of the Bank's liquidity buffers for severe events;
- New **metrics to monitor the profitability of the Bank's business** notably, the **return on required capital** (RoRC)[9] to capture performance at the Bank-wide level and which will

[9] See section 6.2.1.

be used as the measure for the financial objective in the Corporate Scorecard in 2018; and **metrics to assess debt performance through risk-adjusted return on capital**. These allow the assessment of annual portfolio returns as well as projected returns on new projects through a new Investment Profitability Model implemented in 2016.

- The methodical use of **stress test techniques** annually to assess the resilience of the Bank's overall portfolio;
- The articulation of a risk appetite through a **Risk Appetite Statement** introduced during 2016, including a quantification of the risks associated with the Bank's business plan through Financial Loss Tolerance Thresholds; and
- The use of a **Framework for Net Income Allocation Proposals** to guide the formulation of net income allocation proposals.

6.2 Medium Term projections

6.2.1 Financial assumptions

The current expectation is that the key drivers of the Bank's profitability will be broadly similar during the period covered by this SIP to those anticipated in the SIP2017-19.

Debt

- The average margin on performing non-sovereign debt is assumed to weaken slightly to 3.0% reflecting a downward trend in margins on new signings, below the 3.3% average for 2012-2016 and the 3.2% average margins assumed in SIP2017-19. This is driven by market rates and by the planned changes in the regional composition of the portfolio.
- Specific provision charges are assumed at around €0.2 billion per annum for the period 2018-2020, based on Bank's expected loss parameters. This is higher than actual specific provisions in the last five years (2012-2016: annual average €164 million) and reflects a prudent view on long-term default averages. The modelled losses across the planning period results in a projected 7.0% increase in gross impaired debt assets over the period.

Equity

- Overall equity return (dividends received, realised and unrealised gains) is assumed at 6% in 2018 rising to 8% in 2020. Although marginally higher than assumed in the SIP2017-19 (5% in 2017 rising to 7% in 2019), this level is reasonably consistent with actual return in each of the last two years of 8.0%.

Treasury

- Treasury operating income is assumed at €100 million for 2018, €15 million above the budgeted operating income of €85 million in 2017. Income is assumed to increase to €110 million from 2019 onwards. The planned increase across the planning period of 2018-2020 reflects the impact of marginally expanded Treasury activities[10].
- Average weighted investment return on Treasury assets is assumed at 25 basis points (average 2012-2016: 28 basis points).

Other

- Return on capital (and equity cost of funds) is assumed at 0% throughout the SIP2018-20 period based on EURIBOR forward rates. For the purposes of this plan no assumptions are made about an upward path in interest rates.
- Administrative expenditure projections are based on the medium term budget assumptions set out in section 8.1.

10 See *Treasury Enhanced Profitability Initiative* (CS/FO/17-15).

6.2.2 Projected capital growth

The Bank's capital is projected to grow over the SIP2018-20 period by €1.4 billion from €16.0 billion at end 2017 to €17.4 billion by end 2020 as shown in table 6.1.

Table 6.1: Projected growth in capital

€ billion	Actual 2015	Actual 2016	Estimate 2017	Proj. 2018	Proj. 2019	Proj. 2020
Debt return	**0.80**	**0.78**	**0.72**	**0.73**	**0.69**	**0.69**
Impairment charge	0.12	(0.06)	(0.08)	(0.20)	(0.20)	(0.20)
Net (losses)/gains from loans at fair value	(0.04)	0.02	0.03	0.02	0.02	0.02
Debt return after impairment	**0.88**	**0.74**	**0.67**	**0.55**	**0.50**	**0.51**
Equity return (1)	0.28	0.42	0.39	0.33	0.40	0.48
Treasury operating income	0.19	0.16	0.13	0.10	0.11	0.11
Return on capital	0.00	0.00	0.00	0.00	0.00	0.00
Administrative expenses (incl. depreciation)	(0.44)	(0.47)	(0.42)	(0.41)	(0.41)	(0.42)
Financial reporting adjustments	(0.11)	0.13	0.00	0.00	0.00	0.00
Total net profit before net income allocations	**0.80**	**0.99**	**0.77**	**0.57**	**0.60**	**0.68**
Members' equity (before net income allocations) (2)	**14.95**	**15.61**	**16.16**	**16.49**	**16.94**	**17.51**
Net income allocations	(0.36)	(0.18)	(0.18)	(0.15)	(0.11)	(0.12)
Members' equity (after net income allocations)	**14.59**	**15.43**	**15.98**	**16.34**	**16.83**	**17.39**
Required capital	**11.68**	**11.86**	**11.67**	**11.94**	**12.29**	**12.50**
Return on members' equity (IFRS basis)	5.6%	7.0%	4.7%	3.2%	3.7%	4.1%
Return on required capital						
Annual basis	6.7%	8.8%	6.1%	4.4%	5.0%	5.5%
3 year rolling	*3.7%*	*3.4%*	*7.2%*	*6.4%*	*5.2%*	*5.0%*

(1) Equity return includes dividends, realised and unrealised gains, and equity cost of funds.
(2) Includes an estimated restatement of opening members' equity relating to the implemenation of IFRS9.

The higher than previously projected growth in capital over the planning period (2018-2020) compared to SIP2017-19 is driven by higher assumed equity returns, increased Treasury profitability and lower expenses in euro terms, partly offset by lower assumed debt returns. Lower debt return reflects lower assumed non-sovereign margins and a higher proportion of sovereign debt operating assets.

Return on required capital on a rolling three year basis is projected at 6.5% in 2018, incorporating strong results in 2016, and 5.0% by 2020.

The capital projections also take into account potential future **allocations of net income** to 'other purposes' pursuant to Article 36.1 that would reduce the Bank's capital. Any net income allocation proposals need to be developed under the 'Framework for Net Income Allocation Proposals' ('the Framework'), which has an expectation that at least 75% of the Bank's growth in members' equity should be retained in reserves on a rolling three year basis. For planning purposes, illustrative amounts for net income allocations have been assumed over the period covered by this SIP, representing 20% of projected capital growth across the planning period 2018-2020. Any decisions on Net Income Allocations are taken by Governors on the basis of proposals from the Board of Directors.

6.2.3 Projected capital utilisation 2017 to 2020

The development of the Bank's actual and projected operations and capital utilisation is presented in table 6.2.

Table 6.2: Operational and capital utilisation trends

Planning rate (1) € billion (other than percentages)	2015 Actual	2016 Actual	2017 Estimate	2018 Proj.	2019 Proj.	2020 Proj.
Annual Bank investment	9.4	9.4	8.9	9.0	9.1	9.1
Portfolio	41.6	41.8	40.7	41.5	42.7	43.6
Operating assets at cost (prior to accumulated specific provisions)	28.6	29.7	29.2	29.6	30.2	30.7
Statutory capital:						
Prior to specific provisions	40.0	40.4	41.5	41.9	42.2	42.6
Accumulated specific provisions	0.8	0.8	0.8	0.9	1.0	1.1
Total statutory capital	**39.2**	**39.6**	**40.7**	**41.0**	**41.2**	**41.5**
Statutory capital utilisation (2)	**71%**	**73%**	**70%**	**70%**	**71%**	**71%**
Capital adequacy:						
Required capital	11.7	11.9	11.7	11.9	12.3	12.5
Available capital	14.5	15.4	16.0	16.3	16.8	17.4
Capital adequacy utilisation	**80%**	**77%**	**73%**	**73%**	**73%**	**72%**

(1) Actuals at reported rates; projections at planning rate of €/$1.15
(2) Based on both operating assets and statutory capital net of accumulated specific provisions
(See 'Review of the Gearing Ratio Interpretation' (BDS15-018)).

Operating assets are projected to increase from €29.7 billion from the end of 2016 to €30.7 billon at the end of 2020, or an increase of 3%. This planned growth is lower than the previous SIP2017-19 at 10% as described in section 5.2:

- Statutory capital utilisation is projected at 71% by end 2020, well within the 92% prudential threshold.
- Capital Adequacy Policy ('CAP') utilisation is projected at 72% by end 2020, within the 90% prudential threshold. This compares to 81% CAP utilisation at end 2019 projected in the SIP 2017-19.

CAP utilisation is projected to decrease from 77% in 2016 to 72% by end 2020. This pattern is a combination of higher than projected available capital at the end 2016 and a stronger rate of growth in capital relative to required capital across the planning period. On the basis of this higher starting point, the capital base is projected to grow by 13% to end 2020 whilst required capital is only expected to grow by 5% as higher assumed divestments lead to reduced equity exposure together with higher assumed cancellations and prepayments. This is half the rate of growth in required capital when compared to SIP2017-19.

The capital and financial projections incorporate an implied risk profile for the projected portfolio. On the basis of the indicative changes in the regional shares within the portfolio by end 2020 and assuming that the average risk rating for each region remains unchanged, the average capital requirements for debt would be around 20% of debt exposure by end 2020 (September 2017: 21.4%). This primarily reflects a higher projected sovereign share in operating assets.

It can be concluded that the Bank has appropriate capital to support and implement its strategy in the period to 2020, whilst remaining well within the prudential thresholds. There is also capital headroom to support additional operational activity and to absorb variations in projected capital utilisation, for example driven by sensitivities to the EUR/USD exchange rate[11] and the equity portfolio growth and returns.

6.3 Financial resilience

6.3.1 Resilience to stress testing

The Bank conducts stress tests to better understand potential vulnerabilities in its overall portfolio and sub portfolios. The Bank also assesses the impact of stress scenarios on the Bank's projected capital capacity, to understand if the operational plan is within an acceptable risk tolerance and the potential implications of stress events from a capital planning perspective.

To evaluate the robustness of the plan, the stressed parameters from the 'cyclical' (1 in 7 years) and 'severe' stress scenario (1 in 25 years) within the 2017 Annual Bank Wide Stress Test have been applied to the 2018-2020 operational plan. The potential losses and capital implications are assessed against the Bank's risk appetite statement parameters, as discussed in section 6.3.2.

For planning purposes, the Bank's main focus is on the severe scenario. The Bank aims to be sufficiently capitalised to withstand such a severe macroeconomic shock with resulting capital ratios that together with other factors, such as perceived shareholder support, should enable the Bank to retain its triple-A rating[12]. The key impacts of the severe stress can be summarised as follows:

- 3 year cumulative debt losses of €1.3 billion (base case: €0.6 billion debt losses).
- 3 year cumulative equity fair value decline of 42% (base case: 21% growth).
- Broadly 1 notch credit downgrade on all non-defaulted obligors (base case: none).
- Adjustments to operational assumptions: reduced equity divestments, debt prepayments; increased levels of cancellation or restructuring.

In addition, the EUR/USD rate is assumed to depreciate by 29 cents from the planning rate of 1.15 USD per EUR in the SIP to a rate of 0.86 USD per EUR. This assumed strengthening of the dollar raises capital utilisation materially as the value of dollar assets is converted to euro, and then compared against a euro-denominated capital base. This effect is exacerbated when the Bank's capital base is reduced under stress.

An initial assessment of the impact of the stress on the operational plan in the SIP is performed without assuming any proactive reaction to events. The share of new equity in annual Bank investment (ABI) is assumed to remain at 10%, despite the severe economic circumstances modelled. The assumed equity portfolio increases as divestments under stress are presumed to fall, raising the level of equity assets and increasing capital utilisation.

Based on the severe stress and the prudent approach of implementing the original SIP operational plan through the crisis, capital utilisation at end 2020 is projected to be at 95%, compared to 73% at end 2017.

To better reflect reality, the stress test results are mainly assessed by taking into account the effect of the Institutional Actions (IA)[13] that the Bank could take in response to such

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[11] For example, CAP utilisation at end 2020 would increase by 2% if the euro depreciated against the US dollar from the $/€ 1.15 planning rate to a rate of $/€ 1.0 ('parity').

[12] Whilst the aim is to ensure minimum capitalisation, it should be recognised that in such circumstances, retaining a triple-A rating would be particularly subject to qualitative assessment by rating agencies.

[13] Such actions are illustrative and do not prescribe the actions to be taken in the face of a stress scenario.

circumstances. These are relatively limited and include a reduction in the level of net income allocations, reducing the assumed equity share of ABI to 6% (which may in practice prove to be more driven by prevailing market conditions) and a reduction of ABI to €7.5 billion in the second and third year of the stress was assumed. This activity level for new business is consistent with investing through the cycle and avoiding negative signals to rating agencies regarding the Bank's investment capacity and relevance. It is this level of ABI which is used for assessing compliance with the Bank's risk appetite statement parameters (see section 6.3.2).

Table 6.3 shows that:

- If no remedial action is taken in response to the modelled economic shock, the Bank's capital utilisation would still remain below 100%.
- Once Institutional Actions are considered, projected capital adequacy is taken somewhat below utilisation levels that may threaten the Bank's external credit rating and in compliance with the Bank's Capital Adequacy Policy.

Table 6.3: Capital utilisation results – severe stress test

	Peak Capital Adequacy Utilisation	Increase in Capital Utilisation from 2017
Pre-IA Severe with SIP 2017-2019 ABI & equity share 10%	**95%**	**22%**
Post-IA Severe with €7.5bn ABI & equity share 6% for 2019/2020	**88%**	**14%**

In conclusion, the stress test's results suggest that capitalisation levels are strong and the Bank can remain relevant in the event of a severe shock between in the period covered by the SIP.

6.3.2 Risk appetite

In order to ensure that the dynamic between risk taking and capital reserves is prudent, a framework has been established to transparently quantify the level of financial loss that could be experienced (and absorbed) against each operational plan.[14] Such losses and associated capital erosion are assessed under stressed conditions of differing severity. The results are then compared against boundaries, or *Financial Loss Tolerance Thresholds* (FLTT), to ensure the risk associated with each plan is understood and within the expected appetite.

Under the FLTT framework, the Bank looks at the severe[15] and cyclical stress to assess financial performance at different points on the severity distribution. Considering more than one scenario widens the understanding of the Bank's exposure to more predictable downturn conditions, but also against more severely correlated tail-risk shocks.

Table 6.4: Stress Tests Results vs. Financial Loss Tolerance Thresholds

FLTT Metric	Cyclical	Cyclical FLTT	Severe (Post-IA)	Severe FLTT
Net Earnings 1 year (€m)	-1,395	-2,100	-3,406	-3,800
Net Earnings 3 year (€m)	-150	-1,100	-2,676	-3,400
CAP Utilisation 1 year	4%	7%	14%	16%
CAP Utilisation 3 year	4%	10%	15%	20%

The results from these stress scenarios applied to the SIP2018-20 plan are presented below and presented with the FLTT for each respective metric. The improvement in metrics as compared to the 2017 Annual Bank Wide Stress Test is driven both by strengthening in the

14 See Risk Appetite Statement (*CS/AU/17-03*).
15 After the consideration of Institutional Actions.

Bank's current capital position and by adjustments to baseline assumptions about equity divestments and cancellations. The SIP2018-20 plan is within all the risk appetite parameters.

6.4 2018 Financial objectives

6.4.1 Financial performance objectives in the scorecard

The Bank's financial performance will be assessed within the 2018 corporate scorecard through:

- A targeted return on required capital (RoRC) of at least 3.5% (formerly a tracked measure);
- The Bank's realised profit before impairment to be tracked (formerly an objective); and
- Non-sovereign loan impairment ratio (NPL ratio), which is also a tracked measure.

The adoption of a RoRC objective is designed to provide both a more complete picture of the Bank's financial health and appropriate incentives compared to the use of a realised profit goal. The measure is assessed using a three year rolling average basis to moderate the potential volatility, with the minimum return floor reflecting the need for the Bank to build capital over time without disturbing the overall balance within among the elements of the scorecard.

6.4.2 2018 projected income

The base case financial reporting profit before net income allocations is €584 million (see table 6.5).

Table 6.5: Projected income for 2018

	Banking					Treasury	Unallocated	Total
€ million	NS debt	Sovereign	Debt	Equity	**Total**		**items**	
Fee income	111	28	139	0	**139**			**139**
Net interest income	550	41	591	0	**591**			**591**
Net gans from loans at fair value	18		18		**18**			**18**
Dividends			0	92	**92**			**92**
Realised and unrealised equity gains/ (losses)			0	241	**241**			**241**
Treasury investment income						82		**82**
Income from funding activities							18	**18**
Return on capital							0	**0**
Total income	679	69	748	333	**1,081**	82	18	**1,181**
Impairment	(195)	(3)	(198)	0	**(198)**			**(198)**
Risk adjusted return before costs	**484**	**66**	**550**	**333**	**883**	**82**	**18**	**983**
Total administrative costs								(412)
Total net profit (before net income allocations)								**571**
Opening required capital (1)	**5,192**	**829**	**6,021**	**4,189**	**10,210**	**1,281**	**174**	**11,665**
RAROC (before costs)	9.3%	8.0%	9.1%	(2) 8.0%	**8.7%**	6.4%		**8.4%**
RoRC (after full cost allocation)(3)								**4.4%**

(1) Required capital is based on 2017 forecast. Portion for unallocated items is related to operational risk.

(2) Return on capital for 2018 is illustrative based on assumed equity return for the year.

(3) Includes other adjustments to reserves.

Within this:

- Banking is projected to contribute operating income of €1.08 billion before provisions, expenses and return on capital and €883 million after impairment.

- Treasury is projected to contribute operating income of €100 million (of which €82 million income from investment activities and €18 million from funding activities) before provisions, expenses and return on capital.

Overall, the 2018 financial plan shows a 4.5% annual return on required capital (after taking into account expected loss on debt investments as projected impairment and costs):

- Debt is planned to contribute around 56% of the total risk adjusted return before costs (€550 million/€983 million) with a RAROC return before costs of 9.1%. Within the overall debt return, RAROC before costs for non-sovereign debt is projected at 9.3% in 2018. Projected lower returns reflect slightly reduced assumed margins on non-sovereign debt and higher sovereign exposure together with an overall higher required capital.
- The assumed 6% overall nominal equity return is equivalent to 8.0% of opening required capital, which is marginally lower than the projected debt return before costs.
- Treasury investment returns reflect a conservative investment policy; sub-Libor funding benefit is unallocated (no associated required capital).

Of the total projected opening capital employed, 52% relates to debt, 36% to equity, 11% to Treasury and 1% to operational risk.

6.3 Liquidity and 2018 borrowing proposal

The assessment of the Bank's liquidity requirements and derivation of the size of the Borrowing Programme is made annually in the context of each SIP and allows the Bank to plan its liquidity in a medium term context.

The Bank's Liquidity Policy is a key element in safeguarding the Bank's financial stability in the medium term and supports the Bank's triple-A bond rating. The Bank ensures that at any time it is able to meet each of the minimum liquidity requirements set out in the Bank's Liquidity Policy.

This requires that, if the Bank is unable to access the financial markets for funding, liquidity must be sufficient at any given time such that:

- Net Treasury liquid assets are at least 75% of the next two years' net cash requirements;
- At least 12 months of projected net cashflow requirements can be met under an extreme stress scenario; and
- The Bank's liquidity is considered a strong positive factor under the rating agencies' methodologies.

In determining the Bank's liquidity requirements for the following year and deriving the resulting Borrowing Programme, the Bank sets an operating target for liquidity above the minimum policy requirements to retain flexibility in the execution of the Borrowing Programme.

On the basis of the proposed levels of activity in this SIP, **a Borrowing Programme for 2018 of €8.0 billion net new issuance** is set – the same level as 2017. Over the course of 2017, the expected funding level is expected to fully utilise borrowing programme (Actual Q3 2017: €7.2 billion).

It is projected that at the end of 2018 the Bank will have 146% coverage of the next **two years' net cash requirements** (to end 2020), as illustrated in Table 6.6 (2017 estimate: 141%). Within this, projected cash flows from profits largely offset operational cash flow requirements. These cash flows, including within year, remain volatile.

The projected liquidity levels at the end of 2018 aim to ensure the Bank achieves the highest assessment on liquidity from the rating agencies, without targeting a specific rating agency methodology. To support this goal, the Bank uses a **1 year stressed ratio** which broadly ensures that the Bank's liquid funds are sufficient to meets its cash requirements against one year debt service plus 50% of undrawn commitments. The Bank's Liquidity Guidelines require a minimum 100% coverage under this one year ratio at any given time. Coverage under this ratio at the end of 2018 is projected to be around 116% (End 2017 estimate: 113%).

Table 6.6: Projected 2018 year end liquidity ratio

	Year end 2018	Year end 2019	Year end 2020	Aggregate 2019-2020
€ billions				
Opening Gross Treasury liquid assets	**25.6**			
Less short-term debt	(7.1)			
Opening Net Treasury liquid assets	**18.5**			
Movements in the year:				
Net operational disbursements and profit, net of net income allocations	0.2	(0.1)	0.0	(0.1)
Scheduled debt redemptions (incl. new issuance)*	(6.7)	(6.4)	(7.2)	(13.6)
Net annual cash requirements	**(6.5)**	**(6.5)**	**(7.2)**	**(13.7)**
Projected funding level	**8.0**			
Closing Net Treasury liquid assets	**20.1**			

*Combination of remaining 2017 issuance of €2.7 billion and 2018 new funding
Assumption: 30% of new issuance redeemable within 2 years.

	End 2018
Next two years' net cash requirement	(13.7)
Net Treasury liquid assets (includes **€8.0 billion** projected funding)	20.1
Liquidity ratio (min. requirement 75%)	**146%**

The size of the 2018 Borrowing Programme is based on the Liquidity Policy and setting an operating target above the minimum requirements. The projected liquidity also reflects a gradual increase in the size of Treasury exposures funded by medium term debt to support enhanced profitability without a material impact on the risk profile of the overall Treasury portfolio.

This continuation of broadly stable funding levels by the Bank will provide a good signal to the market, whilst ensuring projected liquidity will remain very conservative and prudent. Net Treasury liquid assets are projected to increase from €18.5 billion estimated for end 2017 to €20.1 billion at end 2018.

LEAN AND EFFICIENT ORGANISATION

7. OPERATIONAL EFFECTIVENESS AND EFFICIENCY

The SIP2016-18 set the Bank's aspiration to deliver 'more transition, better'. To help achieve that goal an Operational Effectiveness and Efficiency (OE&E) programme was established with a view to the thorough modernisation of the Bank's processes, procedures and practices. The purpose was to strengthen the Bank to become more responsive to clients; deliver greater impact and value for money for all shareholders, including countries of operations and provide more fulfilling careers for staff.

The OE&E programme is extensive and intricate. It is also a multi-year initiative - designed in 2016, with 2017 seeing the first year of implementation. This section consists of four parts:

- Section 7.1 describes the implementation of the programme in the past year and highlights some of the key initial achievements;
- Section 7.2 reviews the financial implications of the programme over the period covered by this SIP whose results feed into the Bank's medium term budget projections contained in section 8.1;
- Section 7.3 outlines the approach and challenges in developing a robust and modern IT function within the Bank; and
- Section 7.4 reports on the use of the OE&E Budget approved by the Board of Directors in 2017, together with an account of future investment needs.

7.1 Delivery of the programme in 2017

The OE&E programme consists of a set of fifteen integrated workstreams which have been vigorously and effectively taken forward over the year with the support of hundreds of staff across the Bank. This activity is already starting to deliver results. The workstreams are organised in two broad areas.

First, a set of related workstreams which aim at creating effectiveness and efficiency within the Bank's Client Services Group mainly with an external focus. Highlights include;

- A thorough revision of the process and underpinnings of the Bank's country strategies which is the programme's first completed workstream and it is generating multiple advantages: country strategies are more focussed; better grounded in analysis and easier to assess, with preparation time reduced by a third;
- The progressive restructuring of the Banking Department with the creation of a specialised portfolio management function rolled out to cover the Bank's lending for both the corporate sector and Energy and Infrastructure. This has the potential to allow a strengthening of the Bank's ability to support its clients in their business activities and to improve the quality of the Bank's assets over time;
- The streamlining of the transition assessment of projects through the Transition Objectives Measurement System (TOMS) and the development of a standardised set of indicators (the Compendium of Indicators) for assessing projects will support improvements in a number of areas. By simplifying processes, capacity is released to achieve more and better investment and policy activity, strengthening the Bank's overall effectiveness. Over time, the impact of the Bank will be easier to evaluate and communicate. Crucially, this effort supports the embedding of the revised transition concept into the Bank's systems in a way which would have been difficult without the programme; and
- The piloting of simplified approval processes for projects with existing clients will help to make the Bank more responsive to business needs in the financial institutions sector, whilst eliminating repetitive steps from the process for staff. In a similar spirit, experimentation with the greater delegation from the Board of Directors has helped make the Bank more flexible in responding to clients and frees Directors to focus on strategic issues.

The second pillar concerns Business Services and concentrates internally. Work is underway with significant progress, though no workstreams are yet completed. Highlights include:

- Creating a Data Management Function and Governance to bring the coherence to the Bank's records necessary to take full advantage of the new systems of result measurement and client management;

- Streamlined internal decision making to strengthen individual accountability and empowerment within the Bank and support efficiency by reducing unnecessary processes; and
- Piloting and ultimately implementing new ways of working in the Bank's physical space with a view to maximising productivity and creativity.

Taken together, the successful implementation of this programme should modernise both the Bank's approach to its work and its ability to communicate its achievements.

As with all major change programmes, there have been challenges requiring flexibility and adaptability on the part of the Bank to adjust and improve quickly when needed. In a few areas implementation has not fully followed the initial plans. Within the Business Services area, implementation of the procurement workstream has been put back a year. Programme management has put in place a significant course correction in the approach to IT which is described at greater length in section 7.3.

In line with the commitments made in the SIP2017-19, the Board of Directors receives detailed quarterly reporting on the implementation of the programme. This close monitoring and scrutiny has enabled the early identification of emerging issues within the programme.

7.2 The financial impact 2017 to 2020

The previous section outlined the qualitative success to date of the OE&E programme across a number of dimensions. This section provides the latest view of the programmes financial impact, both in the first year of implementation and across the period covered by the current SIP. Table 7.1 shows the pattern of saving – broken down by source - and overall expenditure within the programme to 2020.

Table 7.1: OE&E expenditure and saving 2017 – 2020

Saving (£ million)	2017	2018	2019	2020	Total
Client Services	(5.7)	(9.1)	(9.1)	(9.1)	(33.0)
IT Operating Model	(3.6)	(3.6)	(5.1)	(6.1)	(18.4)
Procurement Operating Model	(0.4)	(0.6)	(1.5)	(1.5)	(4.0)
Saving total	(9.6)	(13.3)	(15.7)	(16.7)	(55.3)
Investment	12.9	11.1	3.7		27.7
Net Investment (saving)	3.2	(2.2)	(12.0)	(16.7)	(27.7)

It shows the strength of the financial case underpinning the programme. The budgeted savings of £9.6 million are in the course of being fully realised in 2017. Looking to the future:

- Savings within CSG at £9.1 million will exceed plan by £0.3 million in steady state and require less expenditure than budgeted on the implementation of the programme;
- The Procurement workstream has the potential for significant further savings from 2019, which could come from user departments benefiting from process improvements and automation. In addition, an effective procurement function is expected to enable better value for money to be obtained in the purchase of goods and services for the Bank;
- The IT workstream sees savings rising from £3.6 million in 2017 to £6.1 million by 2020, against a level of £10.1 million projected in the SIP2017-19.

The table shows that the programme aims at permanently freeing up capacity of £16.7 million by the end of the period or 4.6% of the 2018 budget. On this revised projection the programme fully pays back just over two years, compared to an original pay-back period of exactly two years. This remains an excellent rate of return.

7.3 Reinforcing IT

The IT workstream was always the most complex and ambitious within the programme. It simultaneously requires a major overhaul of the Bank's IT systems, remedying in the process many years of underinvestment, and a fundamental modernisation of the Bank's IT function, including the staffing strategy, to take advantage of the evolving efficiency trends in the industry.

In 2017, following the advice of the Bank's external IT Advisory Board and the appointment of a new Managing Director for IT, significant adjustments have been made to the original plans. While the fundamental direction and building blocks of the original plan are unchanged, this course correction was necessary to ensure both that risks to delivery are managed and new essential investment needs, notably in cyber security, are made. Together, these alterations should support comprehensive and durable change to the IT function.

Work will continue to realise both internal efficiencies and achieving the right balance between permanent Bank staff and contractors. An important component of this is to take advantage of the opportunities provided by outsourcing. This is essential as a means of both realising efficiency gains and benefiting from outside expertise.

In 2017, the first part of a transformation has taken place through which the Bank is becoming equipped to manage successfully the transition from a reliance on in-house skills to using a mixture of external and internal expertise. This work is a precondition of moving in 2018 to outsourcing successfully a significant level of services. Use of the existing OE&E budget is needed to manage this process.

The overall savings from IT related to the full range of activities associated with the OE&E programme are set out in table 7.1. This is composed of a £2.0 million recurrent annual saving from actions implemented in 2017, with the remainder coming from the financial benefits of OE&E investment in the transformation of the IT operating model. Table 7.2 shows the current base case for the pattern of overall investment in this transformation, together with associated savings. These reflect the impact of the linked transformation of the IT organisation and future saving from outsourcing. Table 7.2 shows that this element of the programme alone would pay back in three and a half years. It is important to note that this is the current base case and that there is a degree of uncertainty about both the pattern and scale of expenditure and saving, but the case remains robust. As an illustration, if the whole of the £3.0 million contingency was necessary to deliver the same pattern of savings, the pay-back period would be still reasonable at just over four years.

The level of gross saving from the transformation is also – as reflected in table 7.1 – lower than projected at the time of the SIP2017-19. This reflects a slightly reduced scope for the outsourcing programme; a lower cost of current service provision than previously assessed; a diversification of geographical locations to decrease risk at a higher price and new judgement that the Bank's security costs will need to rise in any event.

Table 7.2: OE&E investment and saving from IT transformation

£ million	2017	2018	2019	2020	Total
Investment	1.4	5.3			6.7
Saving (in addition to recurrent £2 million)		(1.6)	(3.1)	(4.1)	(8.8)
Annual investment (saving)	1.4	3.7	(3.1)	(4.1)	(2.1)
Cumulative investment (saving)	1.4	5.1	2.0	(2.1)	

The SIP2017-19 anticipated that part of the gross savings made by the OE&E programme would be reinvested in IT through offsetting the P&L impact of the programme itself. The thorough review of the IT programme has led to a revisiting of overall financial projections. From this it is evident that the necessary upgrading and continued maintenance of an effective IT function will require the reinvestment of all the savings that might be generated by the programme through IT transformation, including outsourcing. This will support the creation a better skilled; more flexible and more effective IT function, capable of taking advantage of the changing market for IT services, with no increase in budget above 2016 levels.

The SIP2017-19 anticipated that capacity created within IT would be available for use elsewhere in the Bank's budget. The difference in this SIP is accounted for by the combination of the lower level of saving as described above and a realistic appraisal of the cost pressures within the IT function. These have a number of sources

- Higher operating expenditure from the investment in completed projects both those ongoing, such as the support for the implementation of IFRS9, and the OE&E programme;
- Higher than planned depreciation of the same projects, reflecting higher than expected capital costs and increased scope of work;
- The costs of a higher level of activity necessitating greater investment in hardware such as servers and storage capacity, together with the need for a higher level of security; and
- Higher costs for managed services.

In the course of 2018 the objective is to reduce the number of unsupported applications and strengthen the Bank's data analytics capability. Considerable attention and investment will also be on cyber security to ensure the Bank is a cyber risk resilient organisation. The approach during 2018-2019 will be to implement 'secure by design', effective, agile, cost-beneficial and intelligence-led capabilities comprising people, processes and technologies that are adaptable to business, strategic and operational risk management priorities.

In addition, there will be a focus on key OE&E related initiatives, notably the development and initial implementation of the Bank's Project Monarch which will support a new set of systems and applications covering, ultimately, the full range of the Bank's client activities. This shows the interdependencies within the OE&E programme. A successful IT function is the foundation which underpins delivery of savings from other workstreams.

7.4 OE&E expenditure

This section provides details on the usage of the 2017 OE&E budget approved by the Board of Directors together with projected expenditure over future years.

The Board of Directors approved a Budget of £24.0 million to support the OE&E programme for 2017 with overall planned expenditure expected to reach £29.3 million as set out in SIP2017-19.

It is projected that £12.9 million will be spent by the end of 2017. The breakdown of expenditure by area is shown in table 7.3. It also shows projected expenditure for 2018, consisting of three elements:

- £5.3 million to support delivery of those elements of the IT workstream which are known at this stage;
- £2.7 million to support delivery of the programme, including HR support for the major IT restructuring and to bring many of the other workstreams to a successful conclusion in 2018; and
- A contingency buffer of £3.0 million.

Table 7.3: OE&E Expenditure 2017 to 2019

£000	Latest projected expenditure			
	2017 Spend	2018 Spend	2019 Spend	**Total 2017-19**
Client Services	8,753	0	0	8,753
IT Operating Model	1,368	5,278	0	6,646
Procurement Operating Model	614	50	1,018	1,682
Programme management	2,191	2,747	2,673	7,610
Contingency (1)	0	3,000	0	3,000
Total	**12,926**	**11,075**	**3,690**	**27,691**

(1) Use of contingency in 2018 is illustrative

The table also shows an indicative expenditure for 2019 to support the programme, including the delayed delivery of the Procurement workstream, together with a minimal amount in 2018. The current projection for expenditure on the programme is £27.7 million against a projection of £29.3 million in the SIP2017-19. The implications of this pattern of expenditure are shown in Section 8.2.

8. RESOURCING

This section presents the Bank's indicative resourcing needs in order to deliver its objectives for the period covered by the SIP and specific resourcing requests for 2018. For the medium term, there is a particular focus on reviewing and updating the shared understanding between Board and Management of the interaction between the expected savings in the OE&E programme and the Administrative Expense Budget over the period of the SCF. This formed an integral part of the context provided by the SIP2017-19 for approval of the 2017 Budget. This revised profile also directly affects the formulation of the 2018 Budget.

The section is structured as follows:

- Section 8.1 considers the medium term profile of the Bank's Budget;
- Section 8.2 shows the implications for the planned OE&E expenditure in 2018 for the usage of the OE&E investment budget;
- Section 8.3 presents the assumptions on which the proposal for the 2018 Administrative Expense Budget is based;
- Section 8.4 explains the composition and nature of the 2018 Administrative Expense Budget, including the process by which the Budget was formulated; and
- Section 8.5 contains the Administrative Expense Budget and the OE&E Investment Budget; and
- Section 8.6 sets out considerations on the Bank's workforce.

8.1 The medium term profile

The baseline

The Bank committed in the SIP2016-18 to work within a 'flat' budget for 2017 defined as a budget which was no higher in nominal terms than in 2016, excluding increases related to compensation. This set a ceiling on the Budget of £342.9 million prior to any future compensation impacts. The same commitment was made for 2018 in the SIP2017-19. This commitment explicitly assumed no material changes of scope or geography to the Bank's work.

In the course of 2017, Lebanon has become a country of operations and the Bank has become fully active in Uzbekistan after a pause in relations since 2010. Neither of these substantial activities was budgeted for previously. Consequently, the assessment of the medium term resourcing needs and the presentation of the 2018 Budget are based on the assumption that the financing of these activities raises the baseline against which the delivery of the flat budget is assessed. Specifically, this means that the reference point for such an assessment would rise by the full year cost - £4.1 million - of the Bank's work in both countries to a level of £347.0 million. This forms the basis of the approach throughout this section and is highlighted in table 8.3.

Updating the common perspective

In order to maintain the 2017 Administrative Expense Budget (excluding compensation increases) at the same nominal level as the 2016 Budget, £9.6 million of financial capacity released by the OE&E programme was allocated to priority spending. In approving the Bank's 2017 budgets the Board of Directors set the expectation that the total investment made in support of the OE&E programme should be at least fully offset by the creation of incremental available capacity within the budget over the period 2017-20.

The use of such capacity is to be determined by the Board of Directors in the context of annual budget discussions. On the basis of the assumptions prevailing at the time of the discussion of the SIP2017-19, it was expected that the combination of saving and future OE&E capacity creation - the vast majority - would fall just short of that balance by £2.0 million. Management committed to make its best efforts to close the gap over the period.

In order to assess the evolution of the medium terms projections, table 8.1 is taken directly from the SIP2017-19 and sets out the components of the common understanding. Table 8.2 shows the equivalent table based on the revised projections.

In the course of 2017 the Bank's costs have been strictly controlled within the boundaries established by the budgets approved by the Board of Directors. The OE&E programme has delivered across the board, including the savings expected in 2017.

Table 8.2 reflects the revisions that have been made to the design and projected financial impact of the OE&E programme in the course of 2017 and which are described in section 7. As shown there, the most material revision concerns the IT workstream. It is now envisaged that the investment of the budgeted amounts in IT transformation and outsourcing under the OE&E programme will improve the effectiveness and security of the Bank's IT function, but yield lower – yet still adequate – levels of saving.

Further, the table also reflects the use of all of these savings within IT both to support OE&E and other activities. The result of this expenditure will be to modernise the Bank's IT capability and equip it appropriately for the future. As a result of this, the savings of the OE&E programme are fully allocated.

Table 8.1: Indicative unallocated savings in the budget – SIP2017-19

£m	2017 Budget	2018 Estimate	2019 Estimate	2020 Indicative	Total 2017-20
Baseline core budget prior to compensation	***342.9***	***342.9***	***342.9***	***342.9***	
Reduction in core 2017 Budget	**(1.8)**				
Unallocated capacity projected in core budget:					
Net investments in 2017 Budget	11.6	11.6	11.6	11.6	46.4
Incremental SIP16-18 priorities		1.2	1.2	1.2	3.6
OE&E savings	(9.6)	(20.4)	(20.4)	(20.4)	(70.8)
Other Savings	(3.8)	(3.8)	(3.8)	(3.8)	(15.2)
P&L impact of OE&E IT investments		2.1	3.3	3.3	8.7
Use of net savings to reduce 2017 Budget	1.8				
Sub total: Unallocated capacity	**0.0**	**(9.3)**	**(8.1)**	**(8.1)**	**(25.5)**
Total reductions/ unallocated capacity	**(1.8)**	**(9.3)**	**(8.1)**	**(8.1)**	**(27.3)**
OE&E investment budget (maximum envelope)	**24.0**	**4.3**	**1.0**		**29.3**
Difference to baseline	**22.2**	**(5.0)**	**(7.1)**	**(8.1)**	
Cumulative difference to baseline	***22.2***	***17.2***	***10.1***	***2.0***	

Table 8.2: Indicative unallocated savings in the budget – SIP2018-20

£m	2017 Budget	2018 Budget	2019 Estimate	2020 Indicative	Total 2017-20
Baseline core budget prior to compensation	***342.9***	***342.9***	***342.9***	***342.9***	
Reduction in core budget	**(1.8)**				**(1.8)**
Unallocated capacity projected in core budget:					
2017 Budget:					
Net investments	11.6	11.6	11.6	11.6	46.4
Other savings	(3.8)	(3.8)	(3.8)	(3.8)	(15.2)
OEE savings:					
Client Services	(5.7)	(9.1)	(9.1)	(9.1)	(33.0)
IT Operating Model	(3.6)	(3.6)	(5.1)	(6.1)	(18.4)
Procurement Operating Model	(0.4)	(0.6)	(1.5)	(1.5)	(4.0)
Total OEE savings	**(9.6)**	**(13.3)**	**(15.7)**	**(16.7)**	**(55.3)**
2018 Budget:					
Reinvestment in IT		2.7	5.1	6.1	13.9
Use of net savings to reduce Budget	1.8				1.8
Sub total: Unallocated capacity	**(0.0)**	**(2.8)**	**(2.8)**	**(2.8)**	**(8.4)**
Total reductions/ unallocated capacity	**(1.8)**	**(2.8)**	**(2.8)**	**(2.8)**	**(10.2)**
OE&E investment budget (maximum envelope)	**12.9**	**11.1**	**3.7**		**27.7**
Difference to baseline	**11.1**	**8.3**	**0.9**	**(2.8)**	
Cumulative difference to baseline	***11.1***	***19.4***	***20.3***	***17.5***	

Reflecting the magnitude of the deviation from the previous expectations and the importance of successful delivery of the revised plans, the oversight of the Board of Directors of the IT Department and its transformation will be strengthened. Each consideration of the Bank's Quarterly Performance Report will include a separate dedicated discussion of IT. This discussion will be supported by a specific report which will present:

- Key performance information for the implementation of the Bank's IT modernisation programme – 'Tech2020' – and other strategic technology initiatives;
- Advance notice of major investments;
- An account of activities undertaken in the previous quarter and planned in the next period;
- Risks to delivery; and
- An analysis of the costs of the IT function relative to the IT budget.

This discussion will provide Directors with the opportunity to interrogate and understand the implementation of the programme.

It is important to note that the common perspective combines two approaches which are largely distinct. First, the direct return and pay back of the investment itself. As shown here and highlighted further in table 7.1 the programme creates ongoing substantial savings which fully justify the OE&E investment with the rapid recovery of the investment providing an excellent rate of return. It would not be possible to keep the 2017 and 2018 Administrative Expense Budgets below the agreed 'flat budget' baseline without the delivery of the OE&E programme.

The second aspect is the use of the savings. The Bank's budget for 2017 saw the full allocation of the first year of saving - £9.6 million – to a variety of purposes as detailed in SIP2017-19. These decisions were enabled by – but independent from – the savings of the OE&E programme and should not obscure its merits. Overall, in the implementation of the programme:

- Through the direct reinvestment of savings from IT, the Bank will create a robust, flexible function capable of adapting to changing needs and the evolving marketplace at a cost of no more, in nominal terms, than in 2016;
- There is scope for additional efficiencies as the programme is implemented and further developed; and
- As highlighted in section 7.2, the OE&E programme pays for itself in just over two years.

The overall medium term profile

An **Administrative Expense Budget** of £359.5 million has been agreed for 2018, compared to the £346.0 million budget approved for 2017. The proposal complies with the commitment to maintain a 2018 budget at a level no higher than 2016, prior to the impact of compensation adjustments including the impact of foreign exchange movements on existing salaries and prior to additional resources for the changes in the scope of the Bank's activities due to Lebanon and Uzbekistan. As noted in section 8.1, this zero nominal or 'flat' budget formed the basis of the agreement between the Board of Directors and Management for 2017 and 2018.

The SIP2017-19 noted that because inflation, primarily in the UK, has been relatively modest, Management indicated that inflationary and other pressures that increase costs for the same volume of resources could be absorbed within a 'flat budget'. Over the 2017 and 2018 budgets this has resulted in departments absorbing inflationary pressures within their existing budgets, or additional budget having to be provided for specific cost and/or exchange rate impacts. Inflation has increased in the UK and annual Consumer Price Index (CPI) inflation at September 2017 was 3.0%[16]. Cost increases in medical insurance and information costs typically exceed general inflation.

Table 8.3: Projected total administrative expense 2018 – 2020

£m	2016 Restated	2017 Budget	2018 Budget	2019 Estimate	2020 Estimate
Administrative Expense Budget					
(1) Baseline prior to compensation increases					
Admin Exp. Budget prior to compensation	**342.9**	**342.9**	**342.9**	**342.9**	**342.9**
Resources for Lebanon and Uzbekistan			4.1	4.1	4.1
Revised baseline prior to compensation	**342.9**	**342.9**	**347.0**	**347.0**	**347.0**
(2) Adjustments to overall budget					
Reduction in total 2017 Budget		(1.8)			
Illustrative inflationary impact				2.5	5.0
Adjustments to overall budget		**(1.8)**	**0.0**	**2.5**	**5.0**
(3) Cumulative impact of staff cost adjustments					
Compensation adjustments (includes carry over impact)		**4.9**	**12.5**	**18.8**	**25.0**
Administrative Expense Budget GBP	**342.9**	**346.0**	**359.5**	**368.3**	**377.0**
GBP/ EUR rate	1.34	1.16	1.11	1.11	1.11
Admin Expense Budget EUR	**458.8**	**401.4**	**399.0**	**408.8**	**418.5**
OE&E Investment Budget					
Anticipated expenditure (£27.7m aggregate) GBP		12.9	11.1	3.7	
Total actual/ projected expenditure: Administrative Expense Budget + OE&E Investment Budget					
GBP	**341.2**	**358.9**	**370.6**	**372.0**	**377.0**
EUR	**464.7**	**416.4**	**411.9**	**412.9**	**418.5**

Additionally, as described above, the savings from OE&E are proposed to primarily support significant investment and enhancement in IT.

Finally, in the face of these pressures, the 2018 Budget incorporates significant reallocations to enable investment in priority activities (see section 8.4) whilst delivering the agreed 'flat budget'.

The Bank is committed to an efficient use of resources and to strict budgetary control. In recent years, the presentation of the medium term budget against a reference level of the 2016 has been a useful tool for both Board and Management. This approach does not prejudge the future development of the budget over the remainder of the SCF period.

Table 8.3 includes an illustrative development of total administrative expenses to 2020. This incorporates an assumption of a resource base broadly in line with 2016; an inflationary increase of 2.5% is applied to costs other than staff costs and depreciation. These indications, again, do not prejudge the actual course of the budget, but provide a useful long term perspective and inform the multi-year projections contained throughout the SIP.

The projected expenditure over the medium term through the OE&E Investment Budget is presented in Table 7.1 in section 7. The aggregate Administrative Expenditure Budget and

[16] A number of the Bank's contracts incorporate uplifts based on Retail Price Inflation (RPI). At September 2017, annual RPI inflation was 3.7%.

OE&E Investment Budget expenditure for 2018 is £370.6 million or €411.9 million, impacting the Bank's profit and loss account.

8.2 OE&E Investment Budget

An OE&E Investment Budget of £24.0 million was approved by the Board of Directors in 2017. The SIP2017-19 highlighted the fact that any amounts from this budget which was unspent would be carried forward until it was agreed by the Board of Directors and Management that the programme was completed. At this point any remaining budget would be cancelled.

Table 8.4: Projected use of OE&E Budget 2018 – 2020

£000	2017 Budget	2017 Projected Spend	Projected unused budget c/f	2018 Proposed adjustments	2018 Projected Spend
TOTAL	**24,000**	**12,926**	**11,075**	**0**	**11,075**

Table 7.3 showed the utilisation of the OE&E Budget in 2017 and projected expenditure for 2018. Table 8.4 compares that expenditure with the unused amounts from the approved 2017 OE&E budget. On current plans, the unused capacity from the already approved budget for 2017 exactly matches the planned expenditure for 2018. Given this, no further budgetary resources are needed to support the OE&E programme in 2018.

8.3 Basis for the 2018 Administrative Expense Budget

The previous section described the revised profile for capacity creation achieved through the OE&E programme and other means. This capacity is much reduced from that anticipated for 2018 in the SIP2017-19. Despite this, the budget proposed delivers on Management's commitment to achieve a 'flat' Administrative Expense Budget. In order to achieve this, it is proposed that the Board of Directors approves the allocation of the £2.8 million of unallocated capacity identified in section 8.1 to the purposes outlined in section 8.4. Further, the commitment of delivering the flat budget is underpinned by the same assumptions as stated in the previous SIP:

- Increases in staff costs from agreed compensation increases in 2017 and 2018 would be in addition to a flat nominal budget;
- No material changes of scope or geography are made to the assumptions underlying the proposed Business Plan and Budget; and

In addition to these general considerations, specific assumptions are made for the 2018 Budget:

- Those relating to the baseline for assessing whether the 'flat' budget has been achieved were described in section 8.1;
- Those adjustments in costs caused by movements in exchange rates with respect to the part of the budget relating to compensation increases should also be recognised outside the flat budget framework. Depreciation of the pound sterling increases the Bank's costs and appreciation reduces costs.

Foreign exchange movements in 2016 raised the sterling cost of staff expenses in local currency by £3.1 million. At that time it was possible to absorb these costs within the 'flat' budget framework in expectation that there may be a compensating movement in future years. The continued depreciation of the pound sterling has caused a re-examination of that view and motivates the proposal to insulate the 'core' Administrative Expense Budget from the exogenous impact of exchange rate movements, whether positive or negative.

The implications of this for the Administrative Expense Budget are set out in section below.

8.4 2018 Administrative Expense Budget

The proposed Administrative Expense Budget for 2018 is £359.5 million. This consists of a 'flat' budget – after re-baselining for the impact of Lebanon and Uzbekistan - of £347.0 million. In addition, it includes cumulative compensation increases since 2016 of £12.0 million and a further £0.5 million reflecting the impact of exchange rate movements on the sterling cost of compensation costs paid in local currency. The 2018 Administrative Expense Budget represents a nominal increase of 3.9%, including 1.2% increase related to the impact of Lebanon and Uzbekistan.

Table 8.5: Administrative Expense Budget for 2018

Administrative Expenses £m	**2017 Budget**	**2018 Budget**	**2018 vs 2017 £m**	**%**
Operating Expenses	327.6	338.6	10.9	3.3%
Depreciation	18.4	20.9	2.5	13.6%
Admin Expenses GBP	**346.0**	**359.5**	**13.4**	**3.9%**
Exclude:				
Cumulative compensation increases	*(4.9)*	*(12.4)*		
Admin Expenses excl. comp increase	*341.1*	*347.0*	5.9	1.7%
GBP/EUR rate	1.16	1.11		
Admin Expenses EUR	401.4	399.0	(2.4)	-0.6%

In order to contain the necessary and important funding needs within a notional 'flat' budget, significant capacity was freed up through a variety of budget reductions amounting to a total of £10.8 million including £3.6 million incremental OE&E savings. Table 8.6 sets out how these reallocations have been accommodated within the budget. In the areas where the budget is increasing:

- £3.3 million of increases driven by price and foreign exchange (FX) factors (factor (b)). This includes £1.4 million relating to increased medical insurance premiums driven by higher claims, higher retirement plan fees linked to increases in fund sizes, increase of staff costs budget linked to indexation of the Board salaries to UK CPI and increases in information services driven by both supplier increases for core financial and risk data and FX movements. The effect of the depreciation of the pound is reflected in rising non staff expenses, principally the rent of resident offices. Other inflationary impacts will be absorbed within existing budgets.
- £0.9 million of cost increases (factor (c)) are consequences of decisions made in the past. This includes full year impact of the SIP2016-18 resources approved for 2017 and expected higher costs linked to the 2018 location of the Annual Meeting (Jordan). The increased depreciation budget of £0.4 million for the headquarters building reflects the expense consequence of previous capital expenditure[17].
- £3.9 million of increases (factor (d)), including £2.9 million to departmental budgets to support the delivery of the Bank's strategic priorities and £1.0 million to central budgets

[17] This includes the fitting out of the level two of HQ.

for staff separation costs[18] to support ongoing efforts to enhance operational and cost efficiency.

The priorities were identified through a process which initially saw proposals for a total of £6.5 million. These proposals were further assessed, discussed with departments and prioritised. Through this process, the strategic areas for investment contained in this proposal include income generation; further strengthening of equity and portfolio functions; enhancing the capability to assess domiciliation issues; the Bank's local currency and capital market development work, incremental resources for the Human Resources Department and improving the Bank's data management and governance.

Some requests in a number of areas were not funded. Proposed structural changes in HR and potential increases in the per capita training budget were felt to be in need of further development. The resources already devoted to the strengthening of control functions since SIP2016-18 were judged adequate. And a number of proposed additions in CSG were not considered essential at this time.

These budgetary increases have been accommodated by the following budget reductions and reallocations:

- £0.7 million (factor (e)) of budget reduction linked to planned closure of Russia regional resident offices and the Gaziantep RO. The full year impact of closure of the ROs is £0.8 million from 2018 onward.
- £3.9 million total administrative budget released after reviewing of the underlying departmental budgets (factor (f)).

Compensation increases

The 2018 Administrative Expense Budget incorporates an increase of £5.4 million based on the approved staff compensation adjustment and the associated impact on benefits linked to salaries and the performance based compensation pool from 1 April 2018 (the impact for nine months).

For 2019 and 2020, the increase in the overall budget is based on an illustrative compensation adjustment of 3.0% from 1 April each year and the full year impact (the 'carry over' effect) of the 2018 and 2019 adjustments respectively.

In addition, £0.5 million budget is included to reflect the expected adverse impact of foreign currency movements on the staff compensation (for the same volume of resources). To support the agreement around treatment of compensation related increases above the baseline budget, all increases, including the annual impact of the 2017 Compensation and Benefits proposal, are presented separately from the revised baseline budget of £347.0 million[19].

[18] The staff separation costs budget (redundancy and mutually agreed separations) increases to £2.5 million, or 1.8% of the gross salary budget.
[19] Compensation adjustments for the Board of Directors, President and Vice Presidents and the Chief Evaluator are funded within the zero nominal framework.

Table 8.6: Key movements in the 2017 Budget

	£ million	2017	Increase	Reduction	2018
	2017 Budget	**346.0**			
	2017 Compensation & Benefits (9 months phasing)	(4.9)			
	Reversal of 2017 Budget reduction	1.8			
	Resources for Lebanon and Uzbekistan [(1)]	4.1			
a.	**Revised baseline prior to compensation**	**347.0**			
b.	**Price and FX factors:**				
	RO rent		0.4		
	Information services		0.7		
	HQ/RO service charges		0.3		
	Medical insurance		1.4		
	Retirement Plan fees		0.2		
	Rating issuer fees		0.1		
	Board salary increases (CPI)		0.2		
	Sub-total		**3.3**		
c.	**Impact of previous decisions:**				
	Carry over impact of SIP2016-18 priorities		0.2		
	Annual Meeting costs		0.3		
	HQ depreciation		0.4		
	Sub-total		**0.9**		
d.	**Activities prioritised for 2018:**				
	Client Services Group (portfolio, equity, local currency, other)		1.6		
	Risk and Compliance (domiciliation, compliance)		0.4		
	Finance (income generation, data management)		0.3		
	HR and Corporate Services (incl. training, recruitment)		0.4		
	Corporate Strategy		0.1		
	Staff separation costs		1.0		
	Sub-total		**3.9**		
e.	**Russia regional and Gaziantep RO closures**			**(0.7)**	
f.	**Departmental budget reductions:**				
	Client Services Group			(2.8)	
	Risk and Compliance			(0.4)	
	HR and Corporate Services (including IP Programme)			(0.3)	
	Other (OGC, Evaluation)			(0.4)	
	Sub-total			**(3.9)**	
g.	**Other impacts**				
	Capacity from reversing the 2017 Budget reduction			(1.8)	
	Other reductions (centrally managed budgets)			(0.8)	
	Sub-total			**(2.6)**	
h.	**OE&E savings and investments**				
	Client Services Group and Procurement			(3.6)	
	IT Operating Model		2.7		
	Sub-total		**2.7**	**(3.6)**	
	2018 prior to compensation increases		**10.8**	**(10.8)**	**347.0**
	2017 Compensation & Benefits (full year)				6.6
	2018 Compensation & Benefits (9 months phasing)				5.4
	Foreign exchange movement impact on staff costs				0.5
	2018 Budget				**359.5**

Notes:
(1) As detailed in the 2017 Supplementary Budget request (BDS17-108 (Rev), section 2).

Resource reallocations within the Banking Department

The Administrative Expense Budget for 2018 incorporates extensive reallocations across the Bank, as well as a rigorous prioritisation exercise reflecting increased scrutiny of existing departmental budgets (discussed above).

The full upfront implementation of the OE&E programme within the Banking Department of the Client Services Group (CSG) has allowed a thorough overhaul of the structure of the Bank's largest department, promoting significant mobility and refreshment of leadership. This was in addition to the routine flexible reallocation of staff and budgets in response to operational requirements.

Reallocations or adjustments to dedications since the beginning of 2017 have included:

- A total of 67 people left the Bank under the Banking Voluntary Separation Programme. Of the 34 replacements, over 80% were recruited to different or modified roles;
- A reallocation of £1.4 million through the creation of 25 new field based roles in priority regions supported by the cancellation of 20 vacancies across countries of operations;
- Increased support in the field for the core London-based Debt Portfolio Management team - 17 reallocations of which one third were in ROs, including five in Russia.
- Reorganisation of the Equity function with creation of four new field based roles with internal reallocation of the budgets.
- Consolidation of procurement resources within Banking to support the new Procurement Operating Model, leading to twelve staff being reallocated.

Over forty additional reallocations were made within Banking Department reflected in the 2018 Budget proposal, there include increased decentralisation with the transfer of junior banker posts from London to Turkey, Kazakhstan and SEMED; optimisation of the Bank's field presence through transfers to SEMED and EEC from other countries of operations and additional transfers to support the Portfolio Management and Equity groups.

2018 Administrative Expense Budget by expense line

Table 8.7 presents the 2018 Administrative Expense Budget by cost line.

The £9.8 million (4.2%) increase in staff costs is accounted for by:

+ £1.6 million for the full year impact of the 2017 Compensation and Benefits Proposal;
+ £5.4 million to fund the 2018 Compensation and Benefits proposals (including the impact on the Performance Based Compensation (PBC) pool;£0.2 million resulting from the compensation adjustment for the Board of Directors;
+ £0.5 million for the increase in budget caused by the depreciation of sterling against other currencies;
+ £1.4 million additional budget to address medical insurance price increases;
+ £0.2 million additional budget for Retirement Plan administrative fees;
+ £0.2 million carry over impact of the SIP2016-18 priorities approved for 2017;
+ £2.4 million linked to staff cost budget increases to fund incremental priority investments included for 2018 (factor (d) in Table 8.6);
+ £2.8 million incremental budget for Lebanon and Uzbekistan;
+ £1.9 million other increases including the impact of converting some short term roles to regular staff roles;
- offset by a £6.9 million reduction in staff costs budgets as a result of reviewing the departmental budgets (£2.7 million), closure of resident offices (£0.6 million), OE&E (£3.2 million) and other efficiency savings.

Retirement plan related costs are budgeted based on the Bank's cash contributions to the plans. Going forward these costs will be shown as part of total staff costs rather than being separately presented. Historic actual costs and budget data on Board Online Information will be restated to reflect this adjustment. This presentation will also be used in the Quarterly Performance Reports from 2018 onward.

The £2.8 million (6.2%) reduction in non-staff costs:

- £2.7 million reduction in consultancy, mostly due to reclassification of the budget lines in IT budgets (£2.2 million) and review of underlying consultancy budgets in CSG;
- £0.7 million reduction in travel and hospitality costs of the CSG; and

\+ £0.5 million increase in other direct costs, linked mostly to higher market data costs and increased training budget.

The £6.5 million (9.2%) increase of indirect and depreciation costs:

\+ £2.6 million increase in IT and telecommunications mainly due to the reclassification from consultancy costs budget line;

\+ £2.5 million increase in depreciation, of which £1.9 million is linked to IT projects, while £0.4 million relates to HQ occupancy depreciation;

\+ £1.1 million increase in occupancy costs, including £0.4 million FX impact on resident office rents and £0.5 million additional budget required for re-engagement in Uzbekistan and opening of a resident office in Lebanon; and

- £0.3 million additional budget linked to expected higher costs for the Annual Meeting to be held in Jordan. These increases are offset by a £0.1 million reduction in institutional expenditure.

The 2018 Budget incorporates a Management Reserve of £1.0 million. Together with the existing £0.3 million General Contingency (where the use is subject to Board approval), the total contingency funds in the 2018 Budget are £1.3 million, or around 0.4% of the total budget.

Table 8.7: Administrative Expense Budget for 2018

Administrative expenses £m	**2016 Actual**	**2017 Budget**	**2018 Budget**	**2018 £m**	**2018 %**
Total Salary costs	118.4	127.3	130.0	2.8	2.2%
Benefits	46.7	44.6	48.5	3.9	8.8%
Performance Based Compensation	16.5	14.2	14.5	0.3	2.4%
Other Staff Costs	1.8	1.6	1.5	(0.1)	(4.2%)
Retirement Plan	40.4	42.4	45.2	2.8	6.7%
Total Staff Costs	**223.9**	**230.0**	**239.7**	**9.8**	**4.2%**
Consultancy/ Legal costs	24.3	19.2	16.5	(2.7)	(13.9%)
Travel/ Hospitality	9.6	13.3	12.6	(0.7)	(5.2%)
Other Direct Costs	11.2	12.8	13.3	0.5	4.2%
Non Staff Costs	**45.1**	**45.2**	**42.4**	**(2.8)**	**(6.2%)**
Total Direct costs	**269.0**	**275.2**	**282.1**	**6.9**	**2.5%**
Total Occupancy Costs	31.3	31.7	32.9	1.1	3.5%
IT and Telecommunications Costs	13.1	12.3	14.9	2.6	21.5%
Annual Meeting	1.1	1.2	1.5	0.3	22.4%
Central Staff Expenses	5.3	4.7	4.9	0.1	3.2%
Institutional Fees	1.4	2.1	2.0	(0.1)	(6.4%)
Depreciation and Disposal of Assets	20.1	18.4	20.9	2.5	13.6%
Contingency		0.3	0.3	0.0	0.0%
Total Centrally Managed costs	**72.2**	**70.8**	**77.4**	**6.5**	**9.2%**
Admin Expense	**341.2**	**346.0**	**359.5**	13.5	3.9%
GBP EUR rate	1.36	1.16	1.11		
Total Admin expenses EUR	464.7	401.4	399.0	(2.4)	(1%)

Departmental budgets

The total direct costs budget for 2018 of £282.1 million is broken down by department in Table 8.8[20], including the impact of 2018 Compensation and Benefits increases.

- The Banking budget contains a £3.5 million reduction reflecting the full year impact of the OE&E savings, further reduction of the 2018 Budget after review of the underlying budgets (as described in section 8.4) and planned RO closures. This partially offset by £2.8 million addition cost budget for activities in Lebanon and Uzbekistan and increased staff costs from foreign exchange movements.
- To support the Procurement workstream of the OE&E programme, the budgets of two teams have been consolidated within HR & Corporate Services Vice Presidency (VP, HR&CS), resulting in a £1.4 million net transfer of the direct costs budget from Vice Presidency, Policy and Partnerships (VP3). This is partially offset with £0.1 million additional budget for Lebanon. Within an otherwise flat budget for VP3, incremental funding is provided to the LC2 team.
- Direct costs budget of Finance has increased to reflect creation of the Data Management Group and transfer of budgets from Banking and Risk Management departments. It also reflects increased budgets for Treasury in support of work on income generation.
- Increases in HR and Corporate Services, Risk and Compliance as well as OGC reflect incremental total £0.7 million budgets for Lebanon and Uzbekistan.
- It should be noted that unallocated budget includes performance based compensation pool as well as the Management Reserve of the Bank.

Table 8.8: Direct costs by department

Direct costs £m	2016 Budget	2017 Budget	2018 Budget	Variance 17-18
Banking Department	120.9	119.9	119.7	(0.2)
VP, Policy & Partnerships	17.3	18.4	17.3	(1.1)
Client Services Group	*138.2*	*138.3*	*137.0*	*(1.4)*
Finance	14.2	14.6	15.9	1.3
VP, HR and Corporate Service	37.3	29.7	28.3	(1.4)
VP, Risk and Compliance Group	23.7	25.6	27.2	1.5
Office of the General Counsel	17.8	18.8	19.1	0.3
Office of the Chief Economist	1.9	2.3	2.3	0.0
Internal Audit	1.1	1.0	1.1	0.1
President's Office	1.6	1.5	1.6	0.1
Corporate Strategy	1.0	0.9	1.1	0.2
Office of the Secretary General	4.0	4.1	4.2	0.1
Communications	5.6	6.6	6.8	0.2
Evaluation Department	3.1	3.0	3.0	(0.0)
Board of Directors	12.5	12.8	13.1	0.3
Unallocated	18.4	16.0	21.6	5.6
Total Direct costs	280.3	275.2	282.1	6.9

It should be noted that reallocations have been made across the departments to reflect budget reallocations linked to team transfers, as well as the reclassification of IT budgets from non-staff to centrally managed costs category.

Headquarters and resident office resources

Capital expenditure is managed within overall administrative expenditure through adjustments made to the depreciation budget, as approved by the Board of Directors as part of the annual

[20] Historic data is available on Board Online Information

budget. Approximately 80% of the depreciation charges for 2018 come from historic assets. Key areas for capital expenditure planned for 2018 include:

- The reconfiguration of the second floor in 2017 to allow the return of staff from 155 Bishopsgate. This project will also provide a pilot and testbed scheme for the Bank's modern workplace approach. The resulting cost implications will be recognised from 2018 onwards.The work on the Bank's Real Estate Strategic Approach is planned to continue ahead of the expiry of the lease of the HQ building in December 2022.
- Geographical expansion with opening of a resident office in Beirut, Lebanon.
- Reengagement of the Bank's operations in Uzbekistan with new office premises in Tashkent.

In addition, there are planned closures of Russia regional offices in the first quarter of 2018 (Vladivostok, Yekaterinburg, Rostov-on-Don, Samara and Krasnoyarsk) and of Gaziantep RO by end of 2017.

IT resources

The planned spend on IT capital projects in 2018 is around £20-22 million, including:

- £1 million for in flight projects identified as 'business as usual' (IFRS, spreadsheet control and efficiency, Strategic Extranet Project – Phase 2);
- £4 million in flight projects under the OE&E programme (Equity portfolio monitoring and fair valuation, Data Framework, Pegasus);
- £6 million 'business as usual' pipeline projects (Transformation & tech currency, Windows 10 roll out, Cyber security); and
- £9-11 million for pipeline projects under the OE&E programme (Monarch, Procurement and contracting system, Expense Model).

For pipeline projects, the business case, scope and budgets need to be finalised and approved by Management. This includes the scope and cost of the Monarch project, which is under review.

Organisational efficiency

Organisational performance in the Bank's scorecard is measured on the basis of the annual number of operations and the number of operations monitored in the portfolio divided by the actual level of expenditure of the Bank expressed in sterling.

Based on the projected increase of the number of portfolio and new operations and on the projected operating expenditure, the target organisational performance ratio for 2018 is set within a range of 1.7 to 1.9 operations per million pounds (sterling) of operating expenditure.

8.5 2018 Budget Proposals

The Board is asked to approve:

- An Administrative Expense Budget of £359.5 million (€399.0 million) for the Bank's core expenditure, including 2018 compensation proposals; and
- The change of use of £1.7 million (€1.9 million) within the Operational Effectiveness and Efficiency Budget approved in 2017 from FTE related investment to investment in other purposes.

8.6 The Bank's workforce

This section provides an overview of the Bank's staffing and the tools through which it will manage the necessary flexibility in skills, size and shape over the period covered by the SIP.

The table below describes the current composition of the workforce and compares it to the figures of the previous year. There are no significant changes in terms of the relative composition, with approximately half of the organisation employed in the Banking function, and three quarters employed on regular (open-ended) contracts.

Table 8.9: The Bank's Workforce[21]

Numbers and proportions		Prior Year (31 Aug 2016)	Prior Year proportion	This Year (31 Aug 2017)	This Year proportion
Location	HQ	1,767	70%	1,783	70%
	Resident Offices	758	30%	778	30%
Function	Banking	1,356	54%	1,341	52%
	Corporate functions	1,169	46%	1,220	48%
Contract Type	Regular	1,872	74%	1,864	73%
	Fixed term	528	21%	415	16%
	Other	125	5%	122	5%
Job level and gender	Non OTE (male)	1,025	41%	1,036	40%
	Non OTE (female)	892	35%	943	37%
	OTE (male)	97	4%	100	4%
	OTE (female)	511	20%	482	19%

Within these numbers there are some 332 externally funded positions. The 303 of these are financed by donors directly, mainly in support of the Bank's small business programmes. The remainder are financed from the fees paid by donors to defray the costs incurred by the Bank in administering their funds, as required by the Agreement Establishing the Bank. The posts financed from these fees are those which are wholly concentrated on the administration of these funds, although many other staff in the Bank also spend time on this task. In the coming year the Bank will be recruiting thirteen staff to support the effective implementation of projects supported by the Green Climate Fund including policy dialogue, technical assistance and compliance with the demanding legal and administrative requirements of the fund. These will be fully financed from the dedicated management fees received by the EBRD-Green Climate Fund Special Fund.

The Bank's workforce: 2018 – 2020

Delivering stretching business objectives within a flat nominal budget framework for 2018 is becoming ever more challenging. The Bank has adapted to changing demands over time and needs to be able to continue to adapt, given the pace of change in the operating environment. This means examining how work is discharged and how its workforce is allocated to business priorities.

The Operational Effectiveness and Efficiency (OE&E) programme is focussed on the first element and an overview of the programme is set out in Section 7.

The Bank's workforce is its most important resource and to meet the challenging external and internal context it needs to be allocated appropriately. Over the next year, the Bank will move to set out a 'strategic workforce planning' system, which would provide a set of processes to ensure that resources with the right skills are planned for, recruited, reallocated, reassigned, outsourced and terminated, in a way which maximises delivery on operational strategy and objectives. Such resources will need to be flexible enough to support short term needs and changes, whilst anticipating and planning for the longer term. HR has started working with the Bank's Operations, Budget and Strategic Departments to define the steps in this system.

In addition, a permanent organisational development unit will be established in the HR department to promote continuous adaptation to evolving circumstances, recognising that

[21] Figures from The Workforce Information and Review of Market Pay Levels paper *CS/BU17-18*

employees are the Bank's main assets. Early activities will include reviews of structures, roles and processes, to assist with adjustments and changes where needed.

Employee engagement

A key focus will remain raising employee engagement with the aim of improving business performance and efficiency. To support this, the Bank will continue to work with Gallup, a world-leading provider in engagement and strengthening performance management. Their survey and action planning methodology will allow engagement levels and progress against actions plans to be measured and further areas requiring improvement at local line management and organisational levels to be identified. Action planning will be continuous and integrated into day-to-day practices.

Diversity and inclusion

The Bank is committed to building a diverse and inclusive culture and workforce to increase creativity, innovation and promote better decision-making. The Diversity Steering Group, Employee Networks and Human Resources will continue to proactively work in close partnership to ensure our policies and practices are fair and transparent for all.

The Bank continues to measure diversity using metrics set out in the Talent Strategy. Our Talent Review and Succession Planning processes will be further embedded into the HR Cycle. On gender specifically, we continue to work towards our aspiration of having women in half of all Corporate Leadership Group roles and the Bank will aim for a 50/50 gender balance on succession plans for all CLG roles by the end of 2018.

Appropriate Reward

The approach to reward is to position the Bank competitively against the market, promote high performance and the right behaviours, facilitate mobility and staff development and enable a flexible and effective workforce responsive to changes to business requirements. Reward is communicated in an open and transparent way and is managed following clear and consistent processes.

Ensuring that the Banks total reward offering remains competitive in order to recruit, motivate and retain high performers on a diverse basis to the Bank is a continuing priority during the period covered by this SIP. During 2018, an in-depth review of the Bank's offering will be undertaken to include a review of retirement plans, as well as the Bank's benefits structure. In addition an assessment of the competitiveness of the Bank's salary levels in an international context will be examined.