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DOCUMENT OF THE EUROPEAN BANK  
FOR RECONSTRUCTION AND DEVELOPMENT

# STRATEGY IMPLEMENTATION PLAN 2019 - 2021

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**ABBREVIATIONS**

ABI	Annual Bank Investment	MSME	Micro, Small and Medium-sized
AMI	Annual Mobilised Investment	NPL	Non-Performing Loan
BP	Business Plan	OTE	Overtime Eligible
BAAC	Budget and Administrative Affairs	OE&E	Operational Effectiveness and Efficiency
CA	Central Asia	PO	Policy Objectives
CAP	Capital Adequacy Policy	PPP	Public Private Partnership
CCT	Consultants, Contractors and Temporary Staff	PTI	Portfolio Transition Impact
CEB	Central Europe and the Baltics	RAROC	Risk Adjusted Return on Capital
CPA	Composite Performance Assessment	RoRC	Return on Required Capital
CSDR	Country Strategy Delivery Review	RO	Resident Office
EEC	Eastern Europe and the Caucasus	SCF	Strategic and Capital Framework
EPG	Economics, Policy and Governance	SEFF	Sustainable Energy Financing Facilities
ETC	Early Transition Country	SEE	South East Europe
ETI	Expected Transition Impact	SEMED	Southern and Eastern Mediterranean
FLTT	Financial Loss Tolerance Threshold	SIA	Sustainable Infrastructure Advisory
FOPC	Financial and Operations Policies Committee	SIP	Strategy Implementation Plan
GCF	Green Climate Fund	SME	Small and Medium-sized Enterprises
GEFF	Green Energy Financing Facility	SSF	Shareholder Special Fund
GET	Green Economy Transition	TC	Technical Cooperation
IFI	International Financial Institution	TFP	Trade Facilitation Programme
		VP3	Vice Presidency, Policy and Partnerships

## PRESIDENT'S RECOMMENDATION

The EBRD's medium-term strategic orientation is set out in the Strategic and Capital Framework 2016-20 with the overarching theme of supporting countries of operations in their efforts to 'Re-energise Transition'. The pursuit of this goal is made concrete each year through the Bank's annual planning document – the Strategy Implementation Plan – which provides a three year perspective on the Bank's activities setting the context for the consideration by the Board of Directors of the Bank's annual Administrative Expense Budget and Corporate Scorecard.

This Strategy Implementation Plan 2019-21 is the fourth in the current SCF period and the first to extend beyond its final year. At this stage, the projections contained for 2021 – which will form the first year of the next SCF period – assume that the current strategic orientation of the Bank remains broadly unchanged. This is an assumption for planning purposes only and does not prejudge decisions that shareholders may make in the context of the next SCF. Nevertheless, the proposed Plan shows a significant growth of ambition in support of the Bank's countries of operations and follows a robust and detailed Strategic Review of the Bank's activities in each country.

### A successful Bank

The EBRD continues to deliver effectively on its mandate. The SCF's major themes can be distilled into three categories with strong progress made in each area:

- **Maximising transition impact.** The quality of the Bank's impact through its investment projects both at entry and throughout their life remains at near record levels. This high quality has been maintained even as the volume of the Bank's annual investment has reached its highest levels (€9.7 billion in 2017), confirming the EBRD's ability to deliver both quality and quantity. Impact has also been enhanced through the Bank's increasingly focussed, practical approach to policy reform. This effort – and the achievement of an annual level of Green investment above 40% for the first time – has been supported by long term, multiyear budgetary choices made at the outset of the SCF period, demonstrating the value of consistent focus.
- **Maintaining financial sustainability.** The Bank remains financially strong – a fact confirmed by its consistent stable triple-A rating from all the major credit ratings agencies. Internal stress tests show that the Bank is well capitalised and able to withstand shocks. In addition, the Bank's capital has grown in line with the base case presented in the SCF over the past two years and the three year rolling average return on required capital – the Bank's scorecard measure of profitability – is running at 6% against a floor of 3.5%.
- **Efficient and effective organisation.** The Bank's first major change programme in over twenty years continues to be well implemented creating the ongoing savings which have supported budgetary restraint in the SCF period. It has also led to qualitative improvements in the day to day activities of the Bank to the benefit of clients, shareholders and staff. Partly as a result Staff Engagement – a measure tracked in the Bank's Corporate Scorecard – has been broadly maintained in the face of considerable uncertainty. The creation of a specific standing team focused on organisational design within the Bank's Human Resources function will support an ongoing focus on organisational development, agility and efficiency in future.

### A responsive Bank

Whilst successful, the EBRD is not complacent. This SIP reflects important lessons learned from the management mid-term review of implementation of the SCF that has been discussed

extensively with the Board of Directors and shared with the Bank's Governors. The review found that the Bank is broadly on track with the commitments embodied in the SCF. However, there are three interlinked challenges which emerged from the review:

- **Optimising delivery.** The relative comfort of the Bank's capital position is also a challenge. It suggests that the Bank has the capacity, consistent with its fundamental operating principles and strategic orientations, to do more. Similarly, the slowing of the growth of operating assets over the SCF period – ultimately the driver of the Bank's impact on the ground – requires attention. This implies a need to raise the level of the Bank's activity, the quality of its implementation and its disbursements (particularly in the public sector).
- **Maintaining income.** The pressures on the Bank's key income streams have been highlighted frequently in recent years. Much of the explanation lies in overall economic and monetary conditions, but it is crucial that the Bank remains vigilant to ensure that when improved circumstances for income generation arise, the opportunity is taken. As in the case of optimising delivery, successful income generation is best supported by increasing the quality – in terms of return – and the quantity of the Bank's performing assets.
- **Equity performance.** The SCF set an aspiration that the Bank's equity share would rise, which is unlikely to be met. This partly reflects the stage of the economic cycle for many countries of operations, with high valuations limiting opportunities that combine adequate transition and financial return. But it has also prompted a re-think of the organisation and focus of the Bank's approach to its equity activity.

The Bank is continually learning. It is responding actively to address the above concerns: through incentives and organisational changes to optimise delivery; enhancing the focus on revenue generation and asset preservation and continuing to reinforce and professionalise equity investment.

With respect to optimising delivery, the Bank has taken the additional step of undertaking a thorough **Strategic Review** to identify opportunities to further optimise the Bank's delivery across its countries of operations. This SIP fully incorporates the results of the first phase of this work, including deep analysis of the transition opportunities drawing on the work and experience of the EBRD as well as the insights of national authorities, private sector actors and other multilateral institutions. The work also incorporated the conclusions from six cross cutting thematic discussions with Directors.

### **An ambitious Bank**

The mission of the EBRD is to support the development of sustainable market economies with six key transition qualities – competitive, green, inclusive, integrated, resilient and well-governed. Development and mobilisation of the private sector are key to meeting current global and national challenges as highlighted in the report of the G20 Eminent Persons Group on Global Financial Governance. Consequently, the business model and know-how that the Bank has developed since its creation are more relevant than ever today. The European Commission's framing of preparations for the next Multi-Annual Financing Framework also stresses the need for private sector financing to complement ODA, and for using financial instruments in addition to grants to leverage financing for development. Further, the practical operational approach reflected in the six transition qualities is fully aligned with the delivery of the global objectives set out in the Sustainable Development Goals, supplemented by the commitments at COP21 and in the Addis Ababa Action Agenda.

This SIP envisages the Bank realising its potential through strengthening both the quantity and quality of its work in the coming years. The plan proposes an acceleration of the Bank's work with an ambition to see annual activity rising to €1.4 billion in 2021 – 16% higher than 2017's record levels. The result of this activity and the heightened focus on disbursement and impact is that the projected portfolio and operating assets by the end of the SCF period are both expected to be around 10% higher than that presented in last year's SIP. It will also be supported by strengthened resources for equity work; a new emphasis on the delivery of high quality, privately funded infrastructure and a reinforced presence on the ground with satellite offices opened in five countries and enhanced policy work. The analysis in the Strategic Review shows that these medium term goals are credible, but challenging.

## 2019 – Goals and Resources

This is a plan for quality growth. Over the past two years, the Bank's has proposed a budget which was, excluding the costs of compensation and changes in the Bank's strategy, at the same nominal level as that for 2016. This year's proposal of 2.9% increase in total budget moves marginally away from such an approach. Of this increase, 2.8 percentage points of the increase is accounted for by price increases covering the proposed compensation increase, implementing some of the elements of the Bank's Reward Review and contractually agreed inflation impacts. The remaining 0.1 percentage point of the increase represents the minimum investment in the ambitious programme of growth contained in the plan.

In addition, the proposed business objectives for 2019, set out in the Corporate Scorecard are:

- Expected Transition Impact floor for new projects set at 63;
- Portfolio Transition Impact floor set at 65;
- Number of operations within a range of 385 to 440;
- Annual Bank Investment within a range of €9.6 to 10.6 billion;
- Annual Mobilised Investment floor set at €1.0 billion, with a floor for combined annual Bank and mobilised investment set at €8.8 billion;
- A minimum non sovereign share of Annual Bank Investment of 80%;
- A minimum share of Annual Bank Investment in Green Economy Transition activities of 38%;
- Annual disbursement range of €6.7 to 7.9 billion; and
- A three year rolling average of the Return on Required Capital of at least 3.5%.

This Scorecard combines both higher levels of activity and an enhanced emphasis on the quality and nature of the Bank's work. Management is ambitious and demand driven and has consistently demonstrated that transition business opportunities are taken when they exist. In setting an upper end of the business range of €10.6 billion it has responded to the desire of the Board of Directors for greater ambition. At this potential level – the highest in the Bank's history – the risks to effective delivery are significantly heightened and potential inconsistencies between the various quality and quantity objectives could arise. As a result, in delivering this ambitious plan, the guiding principle will continue to be the maintenance of the quality of the Bank's work. Management will carefully monitor delivery to ensure operational and financial risks are well managed. In the event that there is a tension between the activity and its quality the Bank should, and will, prioritise quality.

The Scorecard also contains the Composite Performance Assessments of the Bank's work for each of the six transition qualities. In addition, following the review of the Bank's projected liquidity requirements within this SIP, a Borrowing Programme for 2019 of €9.0 billion net new issuance is proposed, with formal approval by the Board of Directors requested in a separate recommendation. This level of funding aims to ensure that the Bank at any time

meets its minimum liquidity requirements under its liquidity policy and retains flexibility in the execution of the Borrowing Programme. Based on the assessment of the Bank's liquidity within this document it is considered that the Bank will have the ability to continue as a going concern for the next twelve months and this assessment will underpin the preparation of the Bank's 2018 Financial Statements on a 'going concern' basis.

Accordingly, I **recommend** that the Board of Directors approve together:

- An Administrative Expense Budget of £370.0 million (€421.8 million) for the Bank's core expenditure; and
- A budget of £2.8 million (€3.2 million) which can only be used for the costs of the implementation of the Operational Effectiveness and Efficiency Programme.

I **recommend** that the Board of Directors also approve:

- The parameters and objectives contained in the 2019 Corporate Scorecard; and
- The opening of offices of the Bank in Agadir (Morocco), Ismailia (Egypt), Thessaloniki (Greece), Andijan (Uzbekistan) and Cluj-Napoca (Romania).

**Suma Chakrabarti**

## STRATEGY IMPLEMENTATION PLAN – 2019 to 2021

### 1. INTRODUCTION AND SUMMARY

#### 1.1 Planning at the EBRD

The EBRD's plans the delivery of its mandate as laid out in the Agreement Establishing the Bank and made operational through its revised Transition Concept through two principal processes:

- A Strategic and Capital Framework (SCF) through which the Bank's capital adequacy is assessed and its high level strategic objectives (or directions) are set for a five year period approved by the Bank's Board of Governors; and
- A Strategy Implementation Plan (SIP) in which the Bank's annual operational objectives are set through a Budget and Corporate Scorecard approved by the Board of Directors in the context of a three year rolling business plan.

As the medium-term planning document, the SCF sets any new strategic directions together with specific areas of emphasis for pursuing transition impact in line with the Bank's six transition qualities. To support development of a shared vision of priorities in relation to progress achieved and challenges present in the external context, a Medium-Term Directions paper is prepared for discussion with Governors a year before approval of the SCF.

The SIP is designed to show how the SCF priorities will be pursued and any necessary course corrections, but avoids providing new strategic thrusts unless in response to exceptional events. As a result, the core of the SIP is agreement on a budget and scorecard.

Governors approved the Bank's first SCF in 2015 to run from 2016 to 2020. This document contains the fourth SIP of this SCF period which covers the period from 2019 to 2021 with the result, for the first time, that the period covered by the SIP moves beyond the end of that for the SCF. A new SCF will be approved in 2020 setting objectives for the Bank to pursue from 2021 to 2025. Consequently, for the purposes of this SIP, all projections for the year 2021 are undertaken recognising that the Bank's strategy is open to the possibility of significant change at that time.

#### 1.2 SCF 2016-20: Core objectives and assessment

The SCF set a headline goal of 'Re-energising Transition'. This responded to concerns, highlighted and analysed particularly in the Bank's Transition Report in 2013, that reform momentum and with it transition progress and income convergence was slowing across the Bank's countries of operations. Box 1 summarises the aspirations which the SCF set for the Bank over the period to 2020.

The revised transition concept agreed at the end of 2016 provides a clear framework to guide the Bank's work and for understanding its impact. Importantly, the six transition qualities introduced through the revision – competitive, green, inclusive, resilient, integrated and well-governed - are fully consistent with the internationally agreed objectives set out in 2015 on the Sustainable Development Goals; the Paris Agreement on climate change, and the Addis Adaba Action Agenda.

As part of the commitment to continuous improvement – and recognising the contribution that the EBRD could make to delivering all shareholders' objectives - a mid-term management review of the overall progress of the Bank against the objectives set out in the SCF was

undertaken in the first half of 2018. The review found that the Bank is delivering a high quality and volume of transition impact through a diverse range of activities and projects, including Annual Bank Investment at a new peak in 2017. Significant progress has also been

made in a number of specific priority areas including increasing support for the Green Economy Transition, expanding local currency lending and developing policy capability. The composition of the Bank's activity by region is also broadly in line with the SCF objective that the Bank should focus on countries less advanced in transition, with notable increases in activity in the SEMED region and Central Asia. In other priority regions, progress has been more modest, with activity in Early Transition Countries stable and a fall in the portfolio of the Western Balkans.

#### 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 of the Board of Governors.

The review also identified areas where increased attention is needed. Despite the continued financial strength of the Bank as exemplified by its unbroken sequence of unqualified triple-A ratings, each of the principal sources of the Bank's income is under some pressure. On the debt side, high levels of liquidity have increased the availability of market funding and reduced margins. Associated low policy rates mean that returns on that part of the Bank's capital which is unutilised are negligible. Equally, returns on the Bank's equity portfolio are low by historical standards.

In terms of the SCF objectives set out in Box 1, it was found highly unlikely that the equity share in the Bank's portfolio will rise by the end of the SCF period. Externally, this again reflects the stage of the economic cycle where the search for yield means that prices tend to be high on most metrics and the attractive financial and transition opportunities limited. Internally, the steady restructuring, refocussing and sharpening of the Bank's equity efforts has continued and will only bear fruit in time. Also, although the Bank has been successful in meeting its internal targets for mobilisation of external capital, further efforts will be needed to respond to the international community's emphasis in this area.

Of greatest importance is the review's highlighting of the fact that – despite the relatively high level of ABI – the Bank's portfolio and stock of operating assets had grown only modestly over the SCF period. Compounded by the falling levels of capital intense equity in the

portfolio, capital utilisation has remained relatively low at around 70%. This level of utilisation is more than sufficient to allow the Bank to weather stress events (as shown in section 6.3.1), suggesting that the financial capacity exists for the Bank to undertake more activity to support shareholders' objectives.

In the light of this, a Strategic Review is being undertaken. The purpose is to explore ways the Bank could optimise delivery and impact in its countries of operations, in line with its core operational principles (transition, additionality, and sound banking) and fulfilling the orientations provided by the SCF. The process and methodological approach to the first phase of this work is described in section 5.

The initial results of the Strategic Review and subsequent discussion by the Board of Directors are fully reflected in the projections contained in this SIP. The projections show new, higher levels for ABI and consequent portfolio and operating asset growth than those contained in the SIP2018-20 and are set out in full in section 5.2. This growth is projected to be accompanied by a sharp rise in the number of portfolio operations and a move in the composition of activity towards smaller countries which increase the resource intensity of the Bank's work. The pace at which this growth can be achieved as reflected in the objectives for 2019 – the first year covered by this SIP – has been a keenly debated subject. Management has been concerned about the compatibility of higher levels of investment activity and strengthened quality of delivery, together with the financial and operational risks of a rapid acceleration with a – in real terms – flat level of resources. Of course, the Bank's impact is not exclusively driven by its investment activity, but rather through its ability to combine investment with the targeted policy reform dialogue and – where a case can be made – donor resources. Overall, the plan presented here is designed to secure a significant increase in the Bank's transition impact through to the end of the SCF period through:

- Delivering its strategic objectives – including the commitment to Green investment – in a growing portfolio with a higher proportion of operating assets leading to greater capital utilisation reflecting both higher levels of ABI and stronger implementation and disbursement;
- Continued financial strength with the return on required capital well above its floor levels and steady capital growth in line with medium term projections. The Bank will remain resilient to shocks, whilst maintaining additional capacity to meet shareholders objectives; and
- A minimal level of investment in resources to achieve these goals.

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. The proposed Corporate Scorecard for 2019 is also detailed;
- 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;
- Section 5 gives an account of the conduct and initial results of the Bank's Strategic Review and how these results are reflected in investment and policy 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. This section also sets out the 2019 borrowing programme;

- Section 7 considers the overall balance of the portfolio and its consistency with the strategic objectives set out in the SCF; and
- Section 8 presents the resourcing trends – including the Bank’s approach to its workforce - for the medium term, together with the Administrative Expense Budget for 2019.

## **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 is 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 2019 to 2021.

### **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 is operating well above these floors, with levels standing at 66.0 and 70.3 respectively.

The Bank does not project the future evolution of these measures. However, continuation of a set floor value with methodical 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. These levels are further considered in section 4.2.

### **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%.

**Table 2.1: Capital Utilisation Projections 2016 to 2021**

	Control Level	<u>2016</u> Actual	<u>2017</u> Actual	<u>2018</u> Estimated	<u>2019</u> Projected	<u>2020</u> Projected	<u>2021</u> Projected
<b>Statutory</b>	<92%	73%	70%	72%	76%	79%	81%
<b>Capital Adequacy Policy</b>	<90%	77%	70%	72%	73%	74%	75%

Projections across the period covered by this SIP are shown in table 2.1. They show that capital utilisation will rise on both measures to 2021 reflecting the enhanced level of ambition presented in this document. Nevertheless, in terms of the control framework it is anticipated that the Bank will be well below the ceiling level and sufficiently capitalised to implement its objectives. The underlying calculation of these figures is contained in section 6.

### 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 income before impairments. The measure is intended to give incentives to preserve a healthy balance between costs and income generation with the rolling average designed to smooth fluctuations. Following approval by the Bank's Governors of a change in the calculation and use of this parameter in 2017, the control level was set at 50% with an operational limit of 40%. In the event that the operational level is exceeded, Bank Management is required to 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 the appropriate action. 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 2021 are presented in table 2.2. They show that both parameters are projected to be below the control levels for the entirety of the period covered by this SIP. The current estimate of the level of the cost to income ratio for the end of 2018 is 39.8%, the same level as was projected in the SIP2018-20. However, the outcome at the end of the year is subject to important uncertainties, particularly exchange rate movements which may affect the euro valuation of the Bank's equity portfolio over the remainder of 2018. In the event that the operational level is exceeded at the end of the year, the process approved by Governors and described above would be followed. The projection for the years covered by the SIP shows that by the end of 2019 the rolling average should be well below the trigger level and provides an anchor for future budget planning as shown in Section 8. The cost to income ratio fluctuates during the year and is reported in the Quarterly Performance Report, but it is the level at the end of the year which is used for the purposes of assessing compliance with the overall control framework.

**Table 2.2: Resource Parameter Projections: 2016 to 2021**

	Control Level	<u>2016</u> Actual	<u>2017</u> Actual	<u>2018</u> Estimated	<u>2019</u> Projected	<u>2020</u> Projected	<u>2021</u> Projected
Five year rolling average of:							
<b>Cost to Income ratio</b>	<50%	33%	36%	39.8%	34.5%	33.4%	33.7%
<b>Staff Cost to Total Cost</b>	<70%	66%	66%	66%	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 reflects a balance of the Bank's transition, operational, and financial objectives as well as resourcing and organisational goals. The structure of the 2019 Corporate Scorecard is broadly unchanged from 2018. However, a new objective of achieving a minimum share of non-sovereign lending in ABI has been added to emphasise the commitment to increase the focus on private sector lending in the Bank's work. In addition, the existing quantitative objectives for each of the Bank's qualities, including the important goal for the level of lending to promote the Green Economy Transition, is highlighted explicitly in the scorecard. Explanations for the specific levels within the scorecard are set out in the succeeding sections. The scorecard is presented here for approval by the Board of Directors. As highlighted in section 5.1, the combination of strengthened qualitative objectives; increased investment levels and available resources will make delivering all goals in the Scorecard appropriately challenging. Overall, the Bank can be successful even where some aspects of the Scorecard may not be achieved in full.

The current Scorecard structure was last thoroughly reviewed in 2013 with subsequent revisions approved by the Board of Directors reflecting the introduction of the revised transition concept in 2016 and a new financial measure in 2017. A further comprehensive review will be undertaken in the course of the preparation of the Bank's second SCF with a view to introducing an amended Corporate Scorecard from 2021 onwards.

## Corporate Scorecard 2019

	2019	30/09/2018	2018	2017
	BP and Budget	Actual	BP and Budget	Actual
<b>TRANSITION IMPACT</b>				
Expected Transition Impact	<b>Min 63</b>	66.7	Min 60	67.7
Portfolio Transition Impact	<b>Min 65</b>	70.1	Min 65	70.4
<b>Transition Qualities</b>				
Competitive, innovative economies	<b>CPA*</b>	**	CPA	Good
Share of Projects On Track	<b>Min 75%</b>			
Well-governed economies and firms	<b>CPA</b>	**	CPA	Good
Share of Projects On Track	<b>Min 75%</b>			
Environmentally sustainable, green economies	<b>CPA</b>	**	CPA	Very Good
Share of Projects On Track	<b>Min 75%</b>			
GET ratio	<b>38%</b>			
Inclusive, Gender-equal economies	<b>CPA</b>	**	CPA	Very Good
Share of Projects On Track	<b>Min 75%</b>			
Resilient economies and firms	<b>CPA</b>	**	CPA	Good
Share of Projects On Track	<b>Min 75%</b>			
Well-integrated, connected markets	<b>CPA</b>	**	CPA	Good
Share of Projects On Track	<b>Min 75%</b>			
<b>OPERATIONAL PERFORMANCE</b>				
Number of operations	<b>385-440</b>	261	360-400	412
Annual Bank investment (ABI: €billion)	<b>9.6-10.6***</b>	5.7	8.1-9.0	9.7
Annual mobilised investment (€billion)	<b>Min 1.0</b>	0.6	Min 0.8	1.1
Disbursements (€billion)	<b>6.7-7.9</b>	4.8	5.4-6.7	6.2
Non Sovereign Share of ABI	<b>Min 80%</b>		....	....
<b>FINANCIAL PERFORMANCE</b>				
Return on Required Capital (3 year rolling average)	<b>Min 3.5%</b>	6.0%	Min 3.5%	7.4%
Realised profit before impairment (€million)	<b>Tracked</b>	620	Tracked	634
Non-Performing Loan ratio (non-sovereign %)	<b>Tracked</b>	5.7%	Tracked	4.7%
<b>ORGANISATIONAL PERFORMANCE</b>				
Productivity (number of operations based)	<b>1.6-1.8</b>	**	1.7-1.9	1.7
Staff Engagement Ratio	<b>Tracked</b>	**	Tracked	3.8
<b>RESOURCE FRAMEWORK</b>				
<b>EXPENDITURE</b>				
Administrative Expense Budget				
Euro (million)	<b>421.8</b>	286.8	399.0	399.1
Pound Sterling (million)	<b>370.0</b>	268.4	359.5	341.9
Operational Effectiveness and Efficiency Investment				
Euro (million)	<b>3.2</b>	2.7	12.3	15.1
Pound Sterling (million)	<b>2.8</b>	2.4	11.1	12.9

\* CPA: Composite Performance Assessment \*\* Assessed annually

\*\*\* Up to €0.8 billion in BP2019 fungibility possible once minimum Annual Mobilised Investment achieved.

## OPTIMISING TRANSITION IMPACT

### 3. THE TRANSITION CONTEXT

Each SIP is shaped by the economic and reform context in the Bank's countries of operations. This section briefly reviews the economic backdrop against which this Strategy Implementation Plan has been developed. Structural reform needs are also touched on.

#### 3.1 Economic trends

Growth in the EBRD region rose to 3.8% year-on-year in 2017 – the same as the global average – after several years of weaker performance. The acceleration, now sustained for two years, has been broad-based, with contributions from stronger investment activity and higher exports. In the first half of 2018 annual growth picked up further to 3.8%.

However, average growth in the region may have peaked. Reflecting a deceleration in the growth of global trade and a weakening of the advanced European economies, growth is expected to moderate to around 3.3% in the second half of 2018 and 2.6% in 2019. This level is in line with moderate estimates of the potential medium-term growth in the Bank's region, as discussed in the *Transition Report 2013* and the *Transition Report 2017-18*. These estimates, in turn, reflect the lower levels of productivity growth as well as adverse demographic trends, which are explored in detail in the *Transition Report 2018-19*.

Following several quarters of exceptionally accommodating environment, financing conditions for emerging markets have tightened somewhat and are now – from a historical perspective - broadly neutral. The modest tightening of financing conditions has primarily affected capital flows to economies with underlying weaknesses, notably Argentina and Turkey. The Turkish Lira has been hit hard by a crisis of confidence among investors reflecting concerns about domestic policy and geopolitical risks.

The oil price has remained above the level of US\$70 per barrel of Brent since April 2018 owing to stronger demand, production caps agreed by the OPEC and Russia as well as concerns about supply disruptions. Higher oil prices have supported faster recovery of remittances from Russia to Central Asia, Moldova and the Caucasus.

Faster wage growth – reflecting tighter labour markets – played an important role in explaining stronger-than-expected performance in recent quarters, from Romania to Hungary to Belarus. Yet falling rates of unemployment have not yet led to significantly higher inflationary pressures.

Growth in central and south-eastern Europe and Turkey is projected to moderate in 2018 from high levels seen in 2017. The depreciation of the Turkish lira and rising inflation rate have led to significant policy tightening which will weigh on domestic consumption, the main driver of growth in recent years. Shortages of skilled labour constrain medium-term growth potential in Central Europe. Growth in Russia is projected to remain around 1.5%.

In Central Asia, growth is expected to moderate to around 4.5% in 2018-19 in the light of the need for fiscal consolidation. And growth in Eastern Europe and the Caucasus is projected to increase to 3% in 2018 as the recovery in Ukraine gains momentum.

Growth in the southern and eastern Mediterranean region is projected to increase to around 4.4% in 2018 and 4.8% in 2019 on stronger external demand, a gradual recovery in tourism amid an improved security situation, rising investment and improved competitiveness. This regional growth pattern underpins the Bank's activity.

The outlook is subject to numerous risks. For example, as companies took advantage of favourable financing conditions, corporate debt in the EBRD region increased from around

40% of GDP in 2007 to more than 60%, much of it external and/or denominated in foreign currency or the escalation of trade wars that may lead to damage to global supply chains.

### 3.2 Structural reform trends

Overall, structural reforms in the region have proceeded at a modest speed, with an uneven distribution of progress across economies and the qualities of sustainable market economy.

A number of countries have progressed along the six transition qualities introduced in the Transition Report 2018-18 while no significant declines in transition quality scores have been observed. Conditions for doing business improved further in several countries in Eastern Europe and the Caucasus and South-Eastern Europe, leading to upward revisions to competitiveness scores. The same regions have also seen upward revisions to the integrated index, largely due to improved quality of logistics services and related infrastructure.

Many economies in the EBRD regions made progress along the Green dimension following their ratification of the Paris Agreement and reflecting legislated commitments to reduce greenhouse gas emissions. There has been very modest progress in the financial resilience index, while energy resilience appears to have improved across the EBRD regions. Energy resilience score has been revised significantly upwards in Ukraine following major improvements in the legal and regulatory framework, establishment of an independent sector regulator and further progress with tariff reforms.

## 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 2019.

### 4.1 Transition objectives

2016 saw the approval of a revised transition concept to reflect the six key qualities of a modern, 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.

A key tenet of the revised concept has been a greater emphasis on country context in judging the progress towards transition. This approach has underpinned the development of country strategy objectives which systematically assess:

- 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, including the scope for investment and the availability of committed partners in both the private and public sectors; and
- The **capacity** of the Bank to take advantage of those opportunities, based on its areas of expertise, business model and complementarity to other development finance institutions.

Country strategy objectives are pursued through a combination of investment, policy and technical cooperation activities and are set for a five-year period reflecting the long term

nature of the systemic change which the Bank is trying to promote. Country strategies are complemented by sector and thematic strategies which mainly focus on the means through which the Bank's objectives will be delivered at the country level and which also run for five years. Together this process leads to a set of objectives with countries which are focussed on those areas where the Bank can have the greatest impact. Necessarily, this means that within and across countries the focus on each quality is not uniform.

Each year, progress in pursuing the objectives of the country strategy is assessed through Country Strategy Delivery Reviews (CSDRs) that are discussed thoroughly by the Bank's Directors. These reviews both look at current performance and also highlight the opportunities and challenges to future delivery. Exceptionally, this planning cycle has also benefited from the country analysis conducted as part of the initial stage of the Strategic Review summarised in section 5 which provides more detail on the nature of the activities which the Bank is aiming to undertake over the coming three years.

### **Central Asia**

The Bank prioritises development of more competitive, well-governed, green and integrated economies throughout the region. These qualities are all featured prominently in the latest strategy to be approved, for Uzbekistan. Policy dialogue focuses primarily on strengthening the financial sector and business environment, 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). In parallel, the Bank promotes operational and financial effectiveness and efficiency of municipal infrastructure and utilities. The Bank also targets the deepening of 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. Development of local currency lending is a policy priority objective for Uzbekistan.

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 and engagement with investment councils.

The Bank is placing particular emphasis on supporting a more **integrated** region by concentrating its activities on developing transport infrastructure, including through commercial solutions such as PPPs. 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**

Central Europe and Baltics focus on **competitive, green and resilient** transition qualities (with continued emphasis on **well-governed**), with an overarching objective to support frontier-level innovation and higher-value-added activities given the advanced economies of the countries in this region. These qualities are also featured prominently in the latest strategies to be approved, for Poland and the Slovak Republic, where the Bank purports to enhance private sector competitiveness, advance the privatisation agenda and promote resource efficient solutions, all through advanced financial instruments and structures.

Overall, the Bank aims to address 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. 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 and resilience are central to the Bank's activities in Cyprus and Greece. To support a more **competitive** economy, the Bank's engagement focuses on addressing the high leverage and operational inefficiencies 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 a knowledge-economy through innovation and skills.

The Bank prioritises the **resilience** of the financial sector, aiming to assist the restoration of banks' access to capital markets and the support of market mechanisms to resolve NPLs. The Bank also supports the development of non-bank financial institutions and the diversification of sources of funding for local corporates; and similarly, 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.

As noted elsewhere, new project activity in Cyprus is assumed to cease before the end of the period covered in this SIP in 2020, whilst the activity in Greece will continue to 2025 following approval of Resolution no. 216 by the Bank's Board of Governors.

#### Box 3: Priority Policy Objectives

Following the successful piloting in fifteen countries, medium term policy priorities and annual policy milestones (previously called Policy Objectives) have been expanded to over 30 countries, with Country Strategies helping set the multi-year policy priorities that drive the definition of annual policy milestones. The latter are used as a management tool to provide incentives and monitor delivery. Further strategic fit is ensured through exploring government buy-in as well as cross-leveraging cooperation opportunities with other IFIs.

Each annual policy milestone targets at least one quality and is designed considering key risks to delivery and mitigating factors, as well as funding sources. Most annual policy milestones seek to unlock investment opportunities with links to existing or planned investment activities are also explored and adjusted throughout the year. Monitoring takes place on a quarterly basis with senior management being updated on any major challenges which might require further engagement.

Over the period of the SIP2019-21, medium term policy priorities and policy milestones will continue to be part of the broader effort to enhance the transition impact of the Bank through its operations and engagement with authorities and aligning incentives across the organisation. 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, well-governed** and **green** qualities, in addition to its support of a **resilient** economy in five out of the six countries. For all four 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 promoting rule of law, competition and a level playing field for all corporates in Ukraine. 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, and support commercialisation and restructuring of public entities. Activities range from support for investment councils (Armenia), investor councils and competition authorities (Georgia, Moldova), the law of public procurement (Moldova) and improvement of legislative framework for privatisation and other forms of private sector participation (Ukraine). 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 local currencies. 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 also pursues **inclusion** 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. 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. Strengthening economic governance for greater competitiveness is a priority in Tunisia. 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. In addition, the Bank's **inclusion** agenda is emphasised in all four approved SEMED country strategies.<sup>1</sup> In all countries, the Bank aims at increasing economic opportunities for women and youth; and in Morocco and Tunisia, at reducing regional disparities. In Jordan, providing employment and access to services for refugees is also a priority.

Support for **green** market economies is an objective in Jordan, Tunisia 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. A similar emphasis exists in the Bank's engagement in Lebanon<sup>2</sup>. Green and competitive transition qualities are also the priority for policy objectives in the region.

### **South 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

<sup>1</sup> The Tunisia country strategy was approved in December 2018.

<sup>2</sup> A country strategy for Lebanon will be developed in 2019 with a view to approval in early 2020.

region.<sup>3</sup> Policy priority objectives focus particularly on development of more competitive, integrated and green economies.

### Box 3: 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 one of the instruments for delivering the SCF objective of mainstreaming gender and inclusion (together with the Bank's Economic Inclusion Strategy approved in 2017). External delivery and outcomes of the Bank's work in this area are tracked through the Country Strategy Results frameworks. Internal delivery of strengthened institutional capacity for gender mainstreaming is reported through the Quarterly Performance Report, based on the indicators set out in the SPGE's Monitoring Framework. Some highlights of the Bank's extensive work in this area are:

- 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. In 2018, 19 gender projects have been signed to date, with a strong pipeline of further projects until the end of the year. Of these 19, six address Access to Finance, 11 Access to Skills and Employment and 2 Access to Services. This brings the total of projects with a gender component since 2014 to almost 150.
- Priority Policy Objectives with gender components have been established in Kazakhstan, Turkey, Tajikistan, Kyrgyzstan and Jordan. Furthermore, a gender lens has been introduced to inform the Bank's assessment of Investment Climate Reform challenges and the development of associated policy responses in Eastern Partnership countries.
- Awareness of gender issues in the Bank has been raised and staff capacity to address gender issues in their work strengthened in 2018 through a Policy Academy module on Gender and Inclusion that was attended by almost 100 staff from across the Bank generating material from the event now available on the Bank's intranet pages. Learning events and gender sessions with RO and banking staff continued in 2018 to help Bank staff identify opportunities to add value to clients through gender interventions.
- A range of TC assignments have been undertaken with donor and SSF support, including the promotion of equal and safe access to transport in Egypt and research on, amongst others: 'Masculinities in Transition', the 'Care Economy', Equal Opportunities in Power and Energy in Kazakhstan, and Gender in Agribusiness Supply Chains in Turkey and Uzbekistan.
- Gender has been fully mainstreamed in the design of Energy Efficiency and Climate Change operations with extensive support from donors to integrate Gender Action Plans in E2C2 investments.
- Knowledge products have been produced and disseminated, including on the Women in Business programme in Morocco and a toolkit for policy makers to promote Gender Responsive Investment Climate Reforms.
- Capacity development and training on the Bank's Gender and Economic Inclusion work was additionally provided to Ministries of Education in Serbia and Ukraine, and SECO in Egypt.
- The Bank has collaborated closely with a range of external partners, including justice sector institutions in Jordan, the International Development Law Organisation and the Centre for Women's Studies at the University of Jordan. Partnership signed in 2018 with the International Women in Mining Association provides EBRD clients with access to Association mentoring services and peer learning opportunities.
- Data provision for formulating country and project level indicators has been strengthened. Gender is fully integrated in the revised transition methodology and its operationalisation. Assessments of Transition Qualities (ATQs) have been updated for gender under the 'inclusive' transition quality in line with the updated methodology adopted by EPG.

To make the region more **competitive**, the Bank continues to promote a more dynamic private sector through (i) increasing operational efficiency, promoting (business) 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. This aligns with the Bank's efforts to advance **good governance** by focusing on better corporate governance and improving the investment climate.

<sup>3</sup> A more consolidated approach to the region is expected next year following revision of the North Macedonia country strategy.

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. 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).

### 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

Transition is the first of the five categories presented in the Corporate Scorecard. The 2019 Corporate Scorecard contains 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 SCF document provides for the level of the floor for the Bank's average ETI and PTI to be set each year. It is proposed – for the first time – to set an annual scorecard level for ETI above 60 at a level of 63. In the extensive work which was undertaken in examining the nature of the transition goal in the Corporate Scorecard in 2017 the case was made that the level of 60 represented both a significant level of transition ambition, as well as balancing effectively a set of interacting institutional objectives. In order to allow sufficient data for the assessment of the impact of this change on the incentives within the Bank and its delivery, it is proposed that this level be maintained until the end of the SCF period in 2020. For 2019, no change to the current floor for average PTI of 65 is proposed.

The CPAs were introduced in 2016 to provide a comprehensive means of tracking the extent to which the Bank is supporting delivery at the institutional level across all the transition

qualities. CPAs are composed of a set 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 CPA indicators draw from a Compendium of Indicators that allow for consistency in the choice of indicators for all Bank projects.

The specific **reporting indicators** for each quality remain also largely as in 2018:

- **Competitive, innovative economies:** a hard floor of 75 per cent for successful implementation of operations (both investments and 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 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 engagements) targeting this transition quality. In line with the strategic objective to reach a ratio of GET financing of 40 percent by 2020, the Bank will seek to make progress toward this target from year to year. For 2019, a GET ABI ratio target of 38 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 CO2 emissions reduction and the number of sub-loans financed by GEFs (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 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 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 trade facilitation program transactions supported by partner banks; and a qualitative account of results focusing on policy dialogue and advisory work.

As previously, CPAs will be assessed annually with:

- 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. Progress against some components of the CPAs is also reported in the Bank’s Quarterly Performance Report.

## **5. BANK ACTIVITY**

### **5.1 Strategic Review for optimising the Bank’s activity**

As noted in the Introduction, this SIP is exceptionally supported by the initial results of a Strategic Review undertaken by the Bank with a view to optimising its delivery in its current countries of operations. This section sets out:

- The context for the Review and its place within the Bank’s work programme in the run up to the approval of a new Strategic and Capital Framework in 2020;
- The approach taken to the preparation of the initial part of the Review and whose results are reflected more fully in the next section of this document; and
- The approach to reaching final conclusions from the Review.

#### **5.1.1 Context for the review**

The Mid-term Review of the Implementation of the SCF showed that the Bank is strongly capitalised and has the financial capacity to undertake more investment activity. Accordingly, a Strategic Review is being undertaken to examine the opportunities for, and constraints to, further strengthening transition impact and use of the Bank’s capital.

This work was given further impetus by the discussions amongst Governors at the 2018 Annual Meeting in Jordan. Governors reiterated that the first strategic priority for the Bank was the delivery of maximum impact in its countries of operations, especially over the remainder of the SCF period. The first results were intended to be reflected in the projections of Bank activity for the period covered by the SIP and made concrete in the Business Plan for 2019. Final conclusions of the review are to be incorporated in the EBRD’s Medium Term Directions to be discussed at the Annual Meeting in 2019. Those results will also be reflected in analysis of the Bank’s capital capacity which Governors saw as a necessary part of a pre-feasibility study of expansion of the Bank’s geographical area also for consideration at the Annual Meeting in 2019.

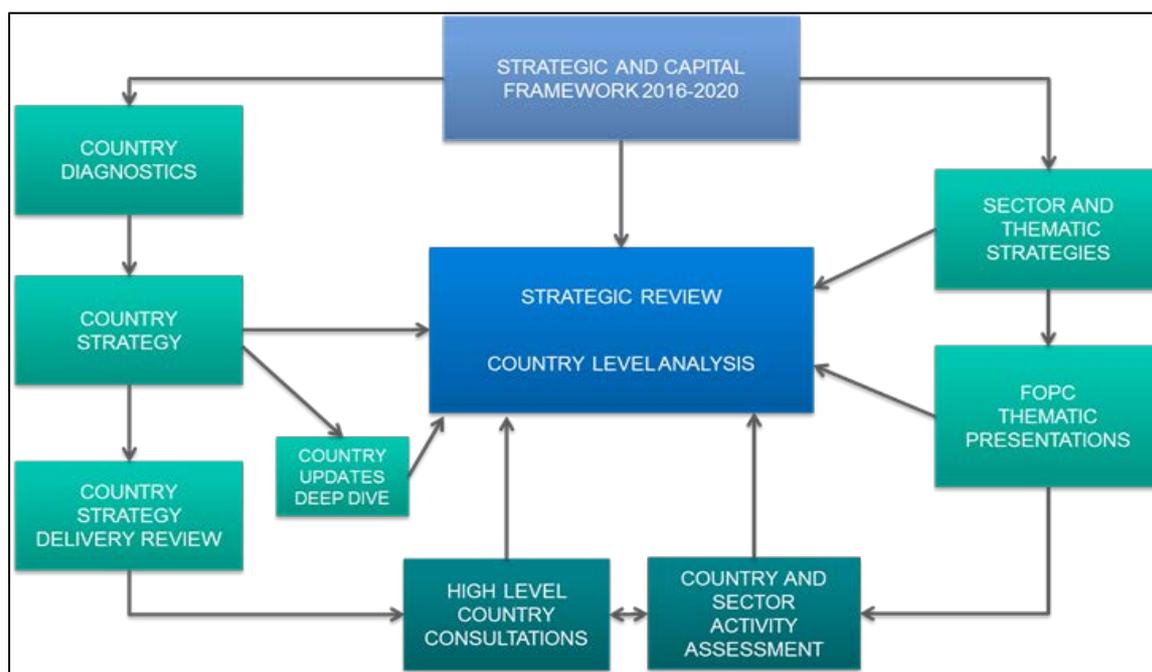
#### **5.1.2 Review framework**

The Strategic Review is a complex and multi-layered exercise. It is founded on three fundamental factors which define the Bank’s mandate and have shaped its distinctive approach:

- The enduring importance of the Agreement Establishing the Bank, including the political principles of Article 1, which provides the underpinning for the Bank’s private sector focus;
- Continued adherence to delivering transition impact through activities which show both sound banking and additionality;
- A transition-oriented private sector development operating model supported by high standards of integrity.

With these foundations in place, the review took place within a structured methodological framework depicted in chart 5.1.

Chart 5.1: Strategic Review: Methodological Framework



As the chart shows, the purpose of the initial phase of the review is to strengthen the implementation of the current SCF to end 2020 with its strategic priority on operating in countries and regions least advanced in transition, notably Early Transition Countries, Western Balkans and SEMED, and sectoral emphasis on Green Economy Transition, sustainable infrastructure, SMEs, local currency and capital markets and equity investment.

### 5.1.3 Country analysis

The country level analysis took account of a range of inputs with the following three specific processes developed specifically for this Strategic Review:

#### High level consultation

A series of high-level consultations were carried out in most countries of operations by the Bank's top management and will continue during the remainder Strategic Review period leading to the 2019 Annual Meeting. These consultations provided the opportunity to discuss with government and the private sector:

- Government priorities and the scope of Bank activity;
- A transition business supportive policy reform agenda;
- The transition business outlook and opportunities;
- The investment climate for the private sector and implications;
- The situation of the banking sector;
- Corporate sector investment trends and Bank products; and
- The potential for SOE restructuring and privatisation.

#### Thematic workstreams

A set of thematic strategic workstreams were also developed. Themes examined included equity, debt income generation, strategic and product innovation, small business, opportunities for wider public sector engagement, and enhancing financing mobilisation. These issues were examined by specialised staff working groups and discussed with Directors in individual FOPC sessions. The findings of this work were taken into account during the

country-level work providing an additional source of guidance for strategic transition business development.

### **Bottom up assessment**

For each country of operations a bottom up assessment was conducted by country and sector teams to identify untapped transition business opportunities. These assessments also drew on analytical material produced by government and other stakeholders, including other multilateral organisations, as well as existing Bank material, notably:

- Country diagnostics including the Assessment of Transition Qualities;
- Country Strategies which have a range of information relevant to the Review;
- For selected larger countries of operations, Country Updates (Deep Dives);
- Country Strategy Delivery Reviews which highlight, in particular, some of the challenges which may have to be considered in optimising delivery; and
- Sector and thematic strategies, such as the Green Economy Transition approach.

#### **5.1.4 Country by country output**

In considering the initial country level results of the Strategic Review, it is important to note that while the formulation of individual country investment ranges reflects a reasonable level of transition, political and economic uncertainty, these ranges assume:

- No additional major political, economic or financial crisis at global or regional levels;
- No major policy change including for example domiciliation or local content preference; and
- No major institutional change in the remit of the EBRD.

Combining all the different inputs and building on these assumptions, a comprehensive analysis for each individual country of operations has been produced which assesses:

- Transition business opportunities;
- An operational activity range based on an assessment of potential eligible demand; and
- External and internal enabling factors underpinning the activity range.

The assessment of eligible demand was carried out in line with the Bank's operating principles and requirements taking account of:

- Government policies and priorities;
- Technical consultations with sectoral ministries on policy and investment programme;
- Market assessments, desktop studies of individual potential market opportunities underpinning business development work including assessment and targeting of potential business opportunities;
- Sustained and proactive dialogue with local and private sector players in the country;
- Empirical feedback from clients and potential investors on market and business opportunities;
- Knowledge building on strong link with main counterparts across EBRD sector activity areas including other IFIs;
- Integrity and reputational risk assessment;
- Staff experience including lessons learned from past experience and knowledge on implementation capacity.

The range of possibilities to expand the level of activity of the Bank, whether qualitatively through policy engagement or quantitatively through investments, depends on a variety of external and internal factors. External factors emerging from the Review across individual

countries include policy related factors such as: specific measures to improve the investment climate, privatisation opportunities, tariff reform, local currency availability, sector policy such as renewable energy framework, or PPP opportunities in infrastructure. Internal enabling factors emerging from the Review include risk appetite, pricing, policy, for example on domiciliation or local content preference, and resources.

Results from individual country reviews were examined by management to ensure consistency with strategy, transition, portfolio risk and financial sustainability. It is important to note that the optimisation of delivery pursued by the Strategic Review includes not only an examination of the quantity of investments which the Bank could make in its countries of operations under certain assumptions, but must also take into account the optimisation of the quality of these investments. Parameters underpinning the quality of investments include, for example, expected and realised transition impact, private sector ratio, equity levels, disbursement rate or Green Economy Transition and inclusion component.

### **5.1.5 Initial results**

The outputs of the individual country-level assessments are aggregated and summarised in the following section of this document. They provide the basis upon which SIP operational, financial and capital utilisation projections are developed for the period 2019 to 2021 and they are supported by the resources proposed in the Administrative Expense Budget for 2019.

In addition to the extensive interaction with the Board of Directors through the development of the Strategic Review, the initial results have already been discussed in three phases through:

- An Executive Session with the Board in mid-September covering proposed country, regional and aggregate activity ranges;
- Two meetings of the FOPC which discussed the Strategic Review reports for the 37 countries of operations; and
- A meeting of the FOPC which examined specific strategic balancing factors and concluded the first phase of the Strategic Review.

### **5.1.6 Next steps**

Following consideration of the initial results of the Strategic Review, a second phase of work is being undertaken which will be incorporated in the Bank's Medium Term Directions to be considered by the Bank's Governors at the 2019 Annual Meeting. The approach to this work will be developed in consultation with Directors in parallel to the consideration of this SIP.

## **5.2 Investment activity**

This section presents the Bank's projected portfolio over the period 2018 to 2021 in line with its strategic objectives and operating principles. This assessment reflects the initial results of the Strategic Review described in section 5.1, details of which are presented in a series of reports covering each country of operations of the Bank. The levels of activity were developed further in discussion with the Board of Directors in the final quarter of 2018. In the course of reaching a plan which could command broad support, it was agreed that:

- The Bank's commitment to the quality of its work would be strengthened through the inclusion in the Corporate Scorecard of a higher level of ETI (as described in section 4.2) a minimum level of non-sovereign investment of 80%, and the explicit inclusion of a GET ratio of 38% ; and
- A headline range of business activity of €9.6 billion to €10.6 billion, together with a set of ambitious operational objectives, notably a step change in the pace of disbursement.

This combination makes delivery on all facets of the scorecard challenging. The pursuit of the top end of the business volume range gives rise to particular potential risks which will need to be carefully managed and were clearly identified by Management in the course of discussions. These include:

- The possibility of an increased number of new transactions and higher levels of active projects in the portfolio without a commensurate increase in resources;
- Increased pressure to promote investment activity, that is ABI, potentially at the expense of the Bank's key operational parameters: sound banking; transition impact and additionality;
- A decrease in the scope for pursuing transition impact through policy work.
- An inherent tension, felt more strongly in some regions than others, between increasing activities while limiting sovereign investment.

Nevertheless, the positive response to the call from the Board of Directors for even greater ambition in the Bank's work is reflected in the following projections:

- The top of the 2019 ABI range is 16.5% higher than that projected in the SIP2018-20 and 12% higher than the estimated 2018 ABI of €9.45 billion;
- The portfolio is projected to be 11% higher than in 2017 by the end of 2019 and 20% higher by the end of the period covered by the SIP, contrasting with a marginal decline between 2015 and 2017;
- The number of operations in the portfolio is projected to be 17% higher than 2017 by 2021;
- The level of the operating assets – and with it impact – is also projected to be 10% higher in 2020 than projected in SIP2018-20;
- Assuming that portfolio quality remains high and operational risks are contained, this could create a solid basis for growth in the Bank's revenues over the period covered by the SIP as outlined in section 6.

This approach reflects the Board of Directors preference expressed in discussions for meaningful and challenging objectives, with the risks associated with them fully understood and accepted. There is a common understanding between Management and the Board of Directors that in the event negative trade-offs between quality and quantity of activity arise, it is the former which will take priority.

### **Annual Activity 2019-2021**

At the end of the third quarter of 2018, Annual Bank Investment was €5.7 billion at the current planning rate, compared to €5.1 billion at end September 2017. Based on the pipeline for the remainder of the year and current conditions, ABI for 2018 is estimated at around €9.45 billion. The projections for the period covered by the SIP reflect the results from the Strategic Review showing a top of the ABI range for 2019 of €10.6 billion further increasing to €10.7 billion in 2020 and €11.4 billion in 2021.

The geographical distribution of the Bank's annual activity levels is projected to be consistent with the Bank's strategic directions and is based on the following assumptions:

- Equity share of ABI is projected at 10%, based on an assessment of the current pipeline and reflecting the Bank's ambition to grow its equity portfolio in support of its transition impact and profitability;
- Sovereign lending is projected at around 18% of ABI reflecting activity in the energy and infrastructure sectors and in line with latest trends;

- Trade facilitation is projected at around 10% of ABI, similar to the level observed in 2017 and in the first eight months of 2018;
- 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 period, no ABI is currently assumed in the SIP 2019-2021 in Russia; and
- New project activity in Cyprus is assumed to cease by end 2020 whilst the Board of Governors has recently extended the Bank's operations in Greece to 2025.

At end August 2018, the number of projects signed was 231 compared to 192 at end August 2017 reflecting a front-loaded distribution of the activity in 2018 compared to previous years and an increase of small and medium-sized projects with the number of projects of less than €10 million increasing by 13% and the number of projects between €10 and €50 million increasing by 43% compared to end August 2017. Based on the current pipeline, the number of operations for 2018 is expected to be around 390 in the upper part of the 2018 Business Plan range. The number of operations is projected in line with the ABI growth during the period and reflects the latest trends in project size composition. Table 5.1 below shows the projected ABI and number of operations for 2018 to 2021. For the purposes of planning, the approach which is taken is to present operational information at both a planning level of ABI of €10.2 billion and an extended upper end of €10.6 billion. The ranges shown for variables in the tables of this section for the years 2019 to 2021 correspond to these two levels of 2019 ABI. The financial projections in section 6 are based on the planning level of 2019 ABI with sensitivities for higher levels of activity for the reasons explained in the introduction to section 6.

**Table 5.1: Number of operations and Annual Bank Investment 2017-2021**

	2017	2018	2019	2020	2021
€billion at planning rate €\$1.15	Act.	Est.	Plan.	Proj.	Proj.
<b>Annual Bank Investment</b>	9.8	9.45	9.6 – 10.6	10.7	11.4
<b>Number of Operations</b>	412	390	385-440	up to 445	up to 470

### Portfolio and Operating Assets Development

Annual disbursement results in 2017 were largely influenced by the back-ended distribution of investment activity during the year. As a result, disbursements in 2017 reached €6.3 billion and end 2017 undrawn commitments started to disburse in 2018 as evidenced by the strong disbursement activity in the first eight months of 2018 which are up 13% from disbursements during the same period in 2017. Reflecting these trends and the projected activity for 2019 to 2021 disbursements are estimated around €6.9 billion in 2018 and projected to increase to up to around €8.7 billion at the end of the planning period.

**Table 5.2: Annual disbursements 2017-2021**

	2017	2018	2019	2020	2021
€billion at planning rate €\$1.15	Act.	Est.	Proj.	Proj.	Proj.
<b>Disbursements</b>	6.3	up to 6.9	up to 7.8- 7.9	up to 8.2- 8.3	up to 8.6- 8.7

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 the main reflow parameters are based on the following assumptions for the period covered by the SIP:

- Future repayment projections are based on 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 2015 to 2017 and to the projected SIP2018-20 level.
- Annual prepayments have continuously declined from a peak in 2016 reflecting a number of large prepayments on projects in Ukraine and the Russian Federation. As a result, the level of annual prepayment decreased from 10% of unimpaired loan operating assets in 2016 to 5% in 2017. The trend in the first eight months of 2018 is similar to that of 2017 and prepayments are projected at around 5% of unimpaired loan operating assets for 2019 to 2021, marginally below the projected level of 6% in the SIP 2018-2020.
- Annual divestments reached €0.4 billion in the first eight months of 2018, below the level of €0.7 billion for the same period in 2017. Based on an examination of the stock of the Bank's current investments and possible exit opportunities, divestments are projected to reach around 14% of equity operating assets in 2018 and are projected at around 13% for the period 2019 to 2021, slightly below the rate of 14% in the SIP2018-20. In volume terms, divestments are projected at around €2.3 billion for the period 2019 to 2021, similar to the levels in SIP2018-20.
- The annual volume of cancellations reached €1.2 billion in 2017, a similar level to 2016. This compared with an average of €0.8 billion over the period 2011 to 2015. Recent trends however show a marked reduction in cancellation activity since the second half of 2017 and at end August 2018, the volume of cancellations was €0.5 billion, 56% lower than the end August 2017 level. Reflecting recent trends, annual cancellations are projected at around 8% of undrawn commitments for the SIP 2019-2021, compared to 10% in the SIP 2018-2020.

As a result of these assumptions, annual reflows are projected at around 15% of total portfolio in 2018 and to remain at around 17% for the period 2019 to 2021.

**Table 5.3: Portfolio reflows 2017-2021**

	2017	2018	2019	2020	2021
€billion at planning rate €\$1.15	Act.	Est.	Proj.	Proj.	Proj.
<b>Portfolio Reflows</b>	6.9	6.5	7.1	7.6-7.7	8.4-8.5

Table 5.4 provides medium term projections for portfolio and operating assets across the Bank's regions of operations resulting from ABI, disbursement and reflow projections. The following portfolio developments are highlighted:

- Reflecting the projected activity levels, the Bank's portfolio is projected to increase by 20% from €42.0 billion at the end of 2017 to €50.2-50.5 billion at the end of 2021;

- Operating assets are projected to grow by up to 22% from €29.0 billion at the end of 2017 to €35.2-35.4 billion by the end of 2021;
- The portfolio in countries other than the Russian Federation is projected to grow by up to 25-26% in the period 2017 to 2021 from €39.1 billion to €49.2-49.5 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 increase by around 18% from around 1,900 at the end of 2017 to up to 2,240-2,250 operations by the end of 2021.

Table 5.4: Portfolio and operating assets 2017-2021

	2017	2018	2019	2020	2021
€billion at planning rate €\$1.15	Act.	Est.	Proj.	Proj.	Proj.
<b>Portfolio</b>	42.0	43.9	46.1-46.5	48.3-48.6	50.2-50.5
<b>Operating Assets</b>	29.0	30.4	32.2-32.4	33.9-34.1	35.2-35.4
<b>Active Portfolio Operations</b>	1,919	up to 2,000	up to 2,085-2,095	up to 2,160-2,170	up to 2,240-2,250

Table 5.5 provides an illustrative projection of the Bank's portfolio regional composition to 2021. This composition reflects strategic portfolio management considerations, the results of the individual Country Strategic Review process described in section 5.1 and requests by a number of Directors for incremental increases in projected activity. 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 as 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.

Table 5.5: Illustrative regional portfolio composition 2017-2021

	2017	2018	2019	2020	2021
€billion at planning rate €\$1.15	Act.	Est.	Proj.	Proj.	Proj.
<b>Central Asia</b>	4.3	4.6	5.0-5.1	5.3	5.5-5.6
<b>Central Europe and Baltics</b>	5.7	5.7	5.7-5.8	5.7-5.8	5.7-5.8
<b>Cyprus and Greece</b>	1.3	1.7	1.9	2.0	2.1
<b>Eastern Europe and Caucasus</b>	7.5	7.8	8.3-8.4	8.8-8.9	9.3-9.4
<b>Russia</b>	2.9	2.2	1.7	1.3	1.0
<b>South-Eastern Europe</b>	7.8	8.1	8.4-8.5	8.6-8.7	8.7-8.8
<b>Southern and Eastern Mediterranean</b>	5.1	6.4	7.8	9.0	9.9
<b>Turkey</b>	7.4	7.4	7.4	7.6	7.9
<b>Total</b>	<b>42.0</b>	<b>43.9</b>	<b>46.1-46.5</b>	<b>48.3-48.6</b>	<b>50.2-50.5</b>

	2017	2018	2019	2020	2021
% Share	Act.	Est.	Proj.	Proj.	Proj.
<b>Central Asia</b>	10%	11%	11%	11%	11%
<b>Central Europe and Baltics</b>	14%	13%	12%	12%	11%
<b>Cyprus and Greece</b>	3%	4%	4%	4%	4%
<b>Eastern Europe and Caucasus</b>	18%	18%	18%	18%	19%
<b>Russia</b>	7%	5%	4%	3%	2%
<b>South-Eastern Europe</b>	19%	18%	18%	18%	17%
<b>Southern and Eastern Mediterranean</b>	12%	15%	17%	19-18%	20%
<b>Turkey</b>	18%	17%	16%	16%	16%

Reflecting these planning parameters, the portfolio projections for 2019 to 2021 show that:

- By the end of the period in 2021, the three largest regional portfolios are projected to be in Southern and Eastern Mediterranean (€9.9 billion), Eastern Europe and Caucasus (€9.3-9.4 billion) and in South Eastern Europe (€8.7-8.8 billion).
- The Central Asia portfolio is projected to grow by 30% from €4.3 billion at end 2017 to €5.5-5.6 billion at end 2021.
- The Central Europe and Baltics portfolio is projected to increase marginally to €7.7-8 billion, reflecting the high maturity level of the Bank's portfolio;
- The Eastern Europe and Caucasus portfolio is expected to grow by around 25% from €7.5 billion to €9.3-9.4 billion in 2021.
- The portfolio in Cyprus and Greece is projected to grow from €1.3 billion to €2.1 billion at end 2021 with a growing reflow rate over the period reflecting the rising maturity of the region's portfolio.
- The portfolio in South Eastern Europe is projected to grow by around 11% from €7.8 billion at end 2017 to €8.7-8.8 billion at end 2021 reflecting the expected flow of new projects in the region over the period covered by the SIP and the advanced maturity of the Bank's assets in the region.
- The Russia portfolio trend reflects, in addition to the expected amortisation of the Bank's portfolio in the country, the impact of portfolio dynamics to date including continuing reflow pressure in the form of divestments and prepayments.
- The portfolio in Turkey is projected to increase from €7.4 billion in 2017 to €7.9 billion at end 2021 reflecting the expected transition opportunities in the country and the growing maturity of the portfolio.

### 2019 Scorecard Parameters

Based on the above projections, the following operational performance ranges are proposed for 2019 to deliver the strategic objectives of the EBRD and to position the Bank on the ambitious portfolio development path emerging from the Strategic Review:

- **Number of operations** range of **385 to 440** reflecting the ABI range and average project size dynamics.
- **ABI** range of **€9.6 to €10.6 billion** reflecting Strategic Review ambition, transition business development activity and the request by a number of Board Directors for incremental ambition in Central Asia, Central Europe and Baltics, Eastern Europe and Caucasus and South Eastern Europe.
- **Annual disbursement** range of **€6.7 billion to €7.9 billion** reflecting 2019 ABI with the lower end reflecting the potential impact of ABI/AMI fungibility.

In 2013, the Board approved the introduction of Annual Mobilised Investment measure alongside an Annual Bank Investment. Since 2014, a floor target for AMI has been set as part of the Bank's scorecard every year. The Board document defines the types of co-financing as qualifying for AMI, reflecting a focus on the Bank earning a fee for raising or administering the funds:

- Loan participations, i.e. B loans;
- Investment cooperation or special funds administered by the Bank or that may become available under the Institutional Investment Partnerships programme; and
- Parallel loans and grants, equity from private equity funds or other sources and non-EBRD portion of structured and capital market products, all subject to a mandate letter and a proportionate specific compensation.

This list did not include two important instruments to mobilise new risk-sharers and investors which are therefore proposed for inclusion in the Bank's Annual Mobilised Investment measure, subject to the principle of proportionate specific compensation:

- Secondary sell-downs of A loans; and
- The mitigation of EBRD risk through the sale of unfunded risk participations (URPs) to third-party financiers.

Taking account of the above AMI approach, it is proposed:

- To further promote the mobilisation of external finance on the Bank's projects by increasing the **fungibility** between EBRD finance (ABI) and Annual Mobilised Investment (excluding unfunded amounts and within same-year sales of A loans) to **€0.8 billion** in 2019 and to increase the total **Annual Mobilised Investment (AMI)** floor to **€1.0 billion** reflecting the impact of unfunded risk participations and sell-downs and the syndication challenges in many of the Bank's regions of operations.
- A combined ABI and AMI floor of **€10.5 billion** to maintain the EBRD operating assets base and revenue generating capacity. Allowing for €0.8 billion of fungibility between EBRD and mobilised external finance results in an ABI range of €8.8 billion to €10.2 billion, with the lower end of the range assuming the maximum fungibility of €0.8 billion.

Discussions continue amongst IFIs on the definition of mobilisation which may lead to future adjustment of AMI for the Bank's scorecard.

**Table 5.7: 2019 Indicative regional and sectoral Annual Bank Investment**

€billion at planning rate €\$1.15	BP2018	BP2019	BP2019	BP2018	BP2019	BP2019
	Indicative Share	Indicative Share Planning Level	Indicative Share Upper End	Indicative Upper End ABI	Indicative Planning Level	Indicative Upper End ABI
<b>Central Asia</b>	11%	13%	14%	1,000	1,350	1,450
<b>Central Europe and Baltics</b>	14%	13%	13%	1,250	1,300	1,400
<b>Cyprus and Greece</b>	7%	5%	5%	610	550	550
<b>Eastern Europe and Caucasus</b>	17%	19%	19%	1,520	1,900	2,000
<b>South-Eastern Europe</b>	16%	17%	17%	1,420	1,700	1,800
<b>Southern and Eastern Mediterranean</b>	18%	24%	23%	1,600	2,400	2,400
<b>Turkey</b>	18%	10%	9%	1,600	1,000	1,000
€billion at planning rate €\$1.15	BP2018	BP2019	BP2019	BP2018	BP2019	BP2019
	Indicative Share	Indicative Share	Indicative Share	Indicative Upper End ABI	Indicative Planning Level	Indicative Upper End ABI
<b>Corporate</b>	25%	25%	25%	2,250	2,590	2,700
<b>Financial Institutions</b>	28%	28%	28%	2,550	2,890	3,000
<b>Energy</b>	24%	23%	23%	2,100	2,360	2,450
<b>Infrastructure</b>	24%	23%	23%	2,100	2,360	2,450

Reflecting discussions at individual country level during the initial phase of the Strategic Review, the indicative geographic and sector composition of annual Bank investment for 2019 is shown in table 5.7.

### 5.3 Donor funding

Donor support plays a vital role in achieving transition impact with such funding enabling important parts of the Bank's investment activity, especially in less advanced transition countries. The Bank's strategic vision for the SCF period is built on its unique private sector

model and sees the Bank as: a selective and strategic user of donor funds; a modern development partner operating in line with international best practice and an efficient manager of a sustainable grant business.

Accordingly, the Bank deploys donor funds selectively, and only where they do not create situations of dependency or distort markets, targeting activities which cannot be undertaken with market instruments alone. Also to ensure the effective and efficient use of concessional resources, the Bank applies the DFI’s blended and concessional finance principles in all its private sector operations.

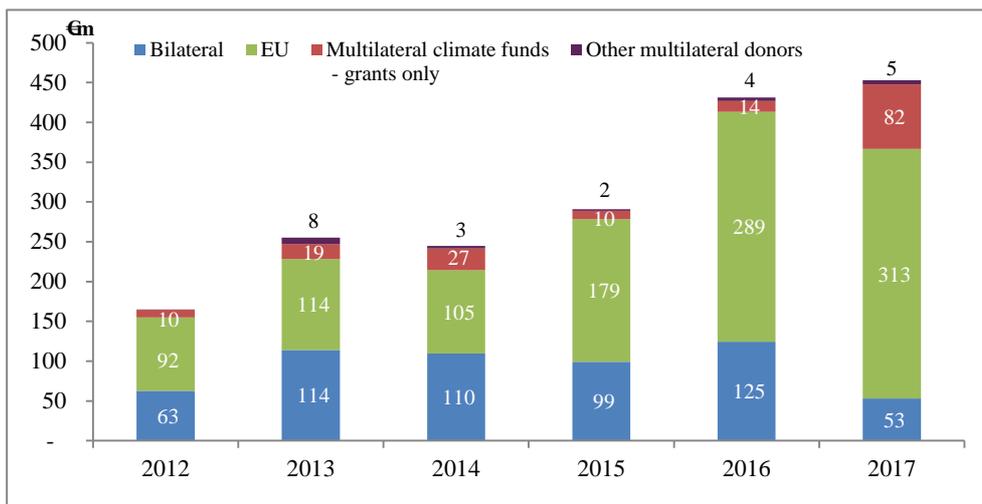
In recent years, the Bank has made significant efforts to improve both its fund mobilisation and offer to donors, resulting in record inflows of donor support. The Bank’s targets in the SCF to date have been fully met, with significant over achievement in 2017, driven mainly by concessional loans from the Green Climate Fund (GCF). This performance has come in an evolving donor landscape, where new donor priorities and funding vehicles are emerging, resources are scarce and competition amongst IFIs with ever converging priorities is on the rise.

The higher level of ambition for investment activity proposed will require a scaling up of the Bank’s fundraising work. The largest proposed increases in ABI relative to previous projections are in the more grant intensive regions including SEMED, Central Asia and EEC. Delivering the higher level of impact will require more implementation support, increased advisory services and a shift towards more GET projects, all of which will require increased donor funding. Meeting these funding needs will require access to both new, and innovative, donor instruments, including blended finance schemes and higher use of risk sharing and guarantee products.

**Recent trends in donor support**

EBRD currently works with some 40 donors, primarily governments and multilateral organisations. Additionally, it receives support through the Bank’s net income mainly via the Shareholder Special Fund.

**Chart 5.2: Grant inflows by source: 2012-2017**



Some key features of the donor landscape in the SCF period are:

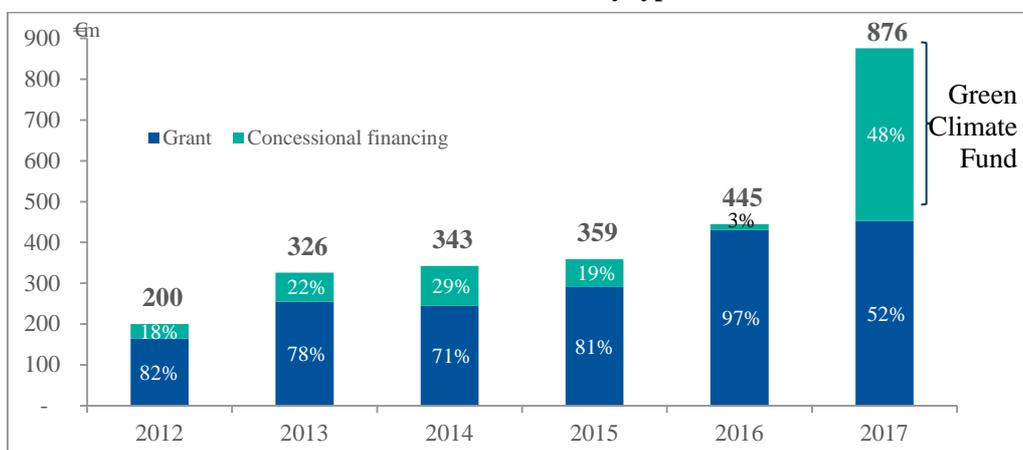
- The EU has emerged as the largest grant donor, providing over two-thirds of grant resources in the past two years. This partnership has continued to evolve, including working with new partners amongst EU institutions and an increased use of financial instruments, such as guarantees.
- The Green Climate Fund is a new donor and also the largest provider of concessional finance to the Bank with a huge increase in 2017 inflows.
- Bilateral donors remain critically important to the Bank, including through support for multi-donor funds. However, their relative share has been decreasing in recent years.
- Countries of operations have shown increased interest in setting up grant funds for use in their respective country. Some examples include Kazakhstan, Albania and Turkey.

The use of donor funds has evolved in parallel with the Bank's business, accelerating post-financial crisis, as the Bank made efforts to strengthen the institutional environment and help the region recover.

In the SCF period the following trends have emerged in the Bank's donor funded activities:

- The majority of transactional grants – 68% - from 2012 to 2016 were used to support GET projects, predominantly in the infrastructure and energy sectors.
- Around one-third of grant earmarks in 2017 were in the FI sector. The majority of these funds were used for risk sharing, incentive payments and TC support for programmes such as GEFF, SEFF and Women in Business. The largest regional recipients of FI project grants were EEC and SEMED.
- Infrastructure remains the sector which uses the most grant resources for technical cooperation with over 300 projects currently undertaken.
- Concessional loans from donors are increasing forming 48% of the 2017 total mainly from the Green Climate Fund.

**Chart 5.3: Donor Fund inflows by type: 2012-2017**



From a regional perspective, grant funds for technical cooperation continue to target less advanced regions in terms of transition level: In 2017, 36% of funds were received for the ETCs, 16% for SEMED and 14% for the Western Balkans.

### Grant intensity

The share of the number of transactions receiving grant support in the SCF period has increased from around 30% to 40%. However, grant intensity in terms of volume remains modest at between 4-5%, up from a level of around 1-2% before 2010. Donor fund usage in private sector operations remains limited. In 2017, EBRD blended about €176 million of concessional finance with its own commercial financing of more than €808 million mobilising €990 million of private finance.

## Future needs

Future needs for donor funding are driven by a number of factors including changes in the level and composition of ABI, new strategic priorities, new partner countries as well as new instruments. In line with this, the Bank identified overall grant funding needs of €1,435 million for 2019. This overall amount includes new instruments such as unfunded guarantees and concessional loans as well as grant needs for a range of sectors and strategic initiatives of the Bank. This translates into an important increase in funding needs compared to 2018, or up some 40%.

Regional needs mostly follow trends in ABI, with needs rising in SEMED, Eastern Europe & Caucasus and South Eastern Europe, while needs are declining in Turkey, Central Europe and Baltics and Cyprus & Greece. Rather counterintuitively, needs are expected to decrease next year in Central Asia, especially in Mongolia, Tajikistan and Uzbekistan, while ABI in the region is expected to pick up. This anomaly could be explained by several reasons: overestimation of needs in the previous year, funding already secured, non-maturity of pipeline, etc.

Projects in support of green transition continue to be highly represented with more than half the total amount expected to support projects targeting the “Green” Transition Quality. As a result, indicative targets for fund raising for the period covered by the SIP are shown in table 5.8.

An indicative target for total donor inflows of **€893 million** has been set for 2019, which represents a similar level as the inflow of donor funds in the exceptional year of 2017. This indicative target includes all donor and grant funding such as official and private-sector co-financing sources, SSF funding, unfunded guarantees as well as concessional finance. An important part of the ambitious 2019 fundraising target is reliant on the Bank securing access to new financial instruments in the form of unfunded guarantees. The identified 2019 targets

**Table 5.8: Indicative fundraising targets 2019-2021 (€million)**

Sources	2019	2020	2021
Donor inflows (including funded and unfunded guarantees)	715	350	350
SSF*	115	100	100
<b>Total non-reimbursable</b>	<b>830</b>	<b>450</b>	<b>450</b>
Donor inflows (reimbursable concessional finance)	63	30	30
<b>Grand total</b>	<b>893</b>	<b>480</b>	<b>480</b>

\* The SSF target for 2019 reflects amounts already approved by Governors composed of €100 million for the ‘core’ SSF and €15 million for the refugee response programme.

for such unfunded guarantees as well as for concessional finance are based on a concrete pipeline of project and programme ideas for which funding is sought. The unfunded guarantee will target programmes in the EEC and SEMED regions with a focus on the GET agenda and the transport and digital sectors. The Bank has been successful in securing pre-approval for an important pipeline of such guarantees. However, as the amounts and timings for these signings are under negotiation and yet to be confirmed, the Bank has chosen a cautious approach and not included the totality of these guarantees within the 2019 target. Like was the case for accessing important levels of concessional finance from the Green Climate Fund in 2017, access to unfunded guarantees is likely to peak in 2019 and subsequently slow down. It is yet too early to assess access to this type of funding in the latter years of the SIP period. This will result in a 2019 fundraising target which is significantly higher than the targets for subsequent years.

While the Bank will continue its current fundraising efforts and maintain close relations with its active donor base through well-established ways of operating, additional efforts will be made to open new doors, test new instruments and new ways of working as per below. In this regard, the Bank will strive to:

- Donors: Broaden the donor base; seek new ways to cooperate with existing donors; explore opportunities with multilateral/global funds which do not yet support the Bank including thematic EU funds; and invest in fund raising from the private sector and philanthropic foundations.
- Instruments: Explore funding for thematic investment platforms also attracting further private sector investments; fine tune and roll-out innovative funding vehicles including portfolio risk-sharing instruments; and explore access to concessional funding from bilateral donors with established soft loan windows, especially related to climate finance.
- Ways of working: Mobilise more support for the Bank's multi-donor funds; invest in local (CoO) fundraising to engage with donors; pilot a multi-year programme for the SSF; and pursue dedicated fundraising campaigns including for key strategic focus areas.

As in previous years, FI and Infrastructure projects make up the bulk of grant needs, together accounting for over 80% of the estimated volume for 2019. Furthermore, projects belonging to the 'Green' Transition Quality continue to be prominent accounting for roughly half the total amount, as in 2018. Indicative fund raising targets for fund raising for 2019-2021 are shown in table 5.8.

## SECURING FINANCIAL SUSTAINABILITY

### 6. FINANCE AND CAPITAL

Financial sustainability is essential to the Bank's continuing ability to deliver its transition mission. The structure of this 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 proposed **2019 financial objectives**; and
- Section 6.5 proposes the level of **the 2019 Borrowing Programme** in order to achieve a prudent level of liquidity by the end of 2019.

The financial assessment of the plan confirms **the Bank has sufficient capital capacity to both support and implement its strategy in the period of this SIP and to withstand potential losses from stress events**. For the purposes of this section the following approach is taken:

- The detailed financial projections are based on the planning level of ABI for 2019 of €10.2 billion. This is taken as a central case and avoids presenting an overly optimistic assessment of future profitability and capital accumulation for planning purposes;
- A sensitivity test is undertaken using the indicative upper end of ABI of €10.6 billion in 2019 to confirm that there is also adequate capital to support this higher level of activity.

In both cases, 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.

## 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.

To support the delivery of these objectives, the Bank has developed tools to **better assess, monitor and manage returns against risk and required capital**, notably:

- The **return on required capital** (RoRC) captures the overall returns on debt, equity and Treasury activities and is used as the measure for the financial objective in the Corporate Scorecard in 2019; and
- The **Investment Profitability Model (IPM)** which allows assessment of projected risk adjusted returns on new projects.

The Bank's existing **financial policies** are supplemented by stress testing. Further, the Bank's high level financial and risk management objectives have been articulated in 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. Finally, a **Framework for Net Income Allocation Proposals** guides the financial assessment of future net income allocations.

## 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 SIP2018-20.

#### *Debt*

- The average margin on performing non-sovereign debt is assumed constant at 3.0% across the planning period. Whilst operating asset margins have tightened in recent years (2016: 3.21%; 2017: 3.11%; Sept 2018: 3.02%), there is some evidence of stabilisation in average margins for new signings (2017: 2.97%; Sept 2018: 2.97%). Although it is too early to tell if this is the beginning of a new trend, indications of changing monetary policy together with the behaviour of debt market spreads and data from the Bank's approved deals support the assumption.
- Net specific provision charges are assumed to be €0.15 billion per annum for the period 2019-2021 consistent with a 5-year average (2013-2017) level of €151 million. Although 2013-2017 covered a period of geopolitical and economic stress to the Bank's region, anchoring the projection in these levels reflects both prudence and the now larger debt portfolio. The assumed losses across the planning period result in a projected 4.7% increase in gross impaired debt assets over the period.

#### *Equity*

- Overall equity return (dividends received, realised and unrealised gains) is assumed at 6% in 2019 rising to 7.5% in 2021 consistent with the assumptions proposed in discussions of the Bank's Enhanced Equity Approach. These levels are in line with the average annual return reported for the last three years (2015-2017) of 6.5% and the projections the SIP2018-20.

### Treasury

- Treasury operating income is assumed at €120 million for 2019, €10 million above the operating income expectations in 2019 of €110 million presented in SIP2018-20. This increase in income is assumed to broadly remain at this level across the planning period, reflecting the implementation of expanded Treasury activities.
- Average weighted investment return on Treasury assets is assumed at 40 basis points (average 2013-2017: 50 basis points).

### Other

- Return on free capital (and equity cost of funds) is assumed at 0% throughout the SIP2019-21 period based on prudent expectations of forward interest rates.
- Administrative expenditure projections are based on the medium term budget assumptions set out in section 8.

## 6.2.2 Projected capital growth

The Bank's capital is projected to grow by €1.8 billion (after net income allocations) from €16.5 billion at end 2018 to €18.3 billion by end 2021 as shown in table 6.1.

**Table 6.1: Projected growth in capital**

€billion	Restated					
	Actual 2016	Actual 2017	Estimate 2018	Plan 2019	Proj. 2020	Proj. 2021
<b>Debt return</b>	<b>0.78</b>	<b>0.76</b>	<b>0.77</b>	<b>0.78</b>	<b>0.81</b>	<b>0.83</b>
Impairment charge <sup>(1)</sup>	(0.06)	(0.00)	(0.16)	(0.17)	(0.16)	(0.16)
Net gains from loans at fair value	0.02	0.01	0.01	0.03	0.03	0.03
<b>Debt return after impairment</b>	<b>0.74</b>	<b>0.77</b>	<b>0.61</b>	<b>0.64</b>	<b>0.67</b>	<b>0.70</b>
Equity return <sup>(2)</sup>	0.42	0.33	0.13	0.34	0.40	0.46
Treasury operating income	0.16	0.11	0.12	0.12	0.12	0.12
Return on free capital	0.00	0.00	0.00	0.00	0.00	0.00
Administrative expenses (incl. depreciation)	(0.47)	(0.42)	(0.40)	(0.43)	(0.44)	(0.47)
Financial reporting adjustments	0.13	(0.02)	0.15	0.00	0.00	0.00
<b>Total net profit before net income allocations</b>	<b>0.99</b>	<b>0.77</b>	<b>0.61</b>	<b>0.66</b>	<b>0.75</b>	<b>0.82</b>
<b>Members' equity (before net income allocations)</b>	<b>15.74</b>	<b>16.35</b>	<b>16.64</b>	<b>17.17</b>	<b>17.77</b>	<b>18.48</b>
Net income allocations	(0.18)	(0.18)	(0.13)	(0.14)	(0.11)	(0.13)
<b>Members' equity (after net income allocations)<sup>(3)</sup></b>	<b>15.56</b>	<b>16.17</b>	<b>16.51</b>	<b>17.03</b>	<b>17.66</b>	<b>18.35</b>
<b>Required capital</b>	<b>11.86</b>	<b>11.35</b>	<b>11.93</b>	<b>12.54</b>	<b>13.09</b>	<b>13.70</b>
Return on members' equity (IFRS basis)	7.0%	5.1%	2.9%	4.0%	4.4%	4.6%
<b>Return on required capital (%)</b>						
Annual basis	8.8%	6.7%	4.1%	5.5%	6.0%	6.2%
3 year rolling	3.4%	7.4%	6.5%	5.4%	5.2%	5.9%

(1) Includes specific and general provision charges.

(2) Equity return includes dividends, realised and unrealised gains, and equity cost of funds.

(3) 2018 reserve movements now include deferred P/L from some hedging activities following the implementation of IFRS 9 Hedge accounting.

The higher than previously projected growth in capital over the planning period (2019-2021) compared to SIP2018-20 is driven by increased anticipated profits from both the Banking debt portfolio and Treasury activities reflecting both an expanded balance sheet and a lower

assumed level of impairment. Return assumptions are broadly unchanged from previous SIP for both of these activities.

The **return on required capital** on a rolling three year basis is projected at 5.4% in 2019, incorporating strong results in 2016 and 2017, and significantly exceeds the minimum 3.5% floor for the remainder of the period covered by the SIP.

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 proposal needs to be developed under the Framework for Net Income Allocation Proposals, 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 broadly 20% of projected capital growth across the planning period 2019-2021. Such illustrative amounts should not be seen as pre-empting any decisions on Net Income Allocations that are taken by the Board of Governors on the basis of proposals from the Board of Directors.

### 6.2.3 Projected Capital Utilisation

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**

<b>Planning rate <sup>(1)</sup></b>	<b>2016</b>	<b>2017</b>	<b>2018</b>	<b>2019</b>	<b>2020</b>	<b>2021</b>
<b>€ billion (other than percentages)</b>	<b>Actual</b>	<b>Actual</b>	<b>Estimate</b>	<b>Proj.</b>	<b>Proj.</b>	<b>Proj.</b>
Annual Bank investment	9.4	9.7	9.5	10.2	10.7	11.4
Portfolio	41.8	41.4	43.9	46.1	48.3	50.2
<b>Operating assets at cost (prior to accumulated specific provisions)</b>	<b>29.7</b>	<b>28.7</b>	<b>30.4</b>	<b>32.2</b>	<b>33.9</b>	<b>35.2</b>
<u>Statutory capital:</u>						
Prior to specific provisions	40.4	40.9	41.8	42.2	42.6	43.0
Accumulated specific provisions	0.8	0.6	0.7	0.8	0.8	0.9
<b>Total statutory capital</b>	<b>39.6</b>	<b>40.3</b>	<b>41.1</b>	<b>41.4</b>	<b>41.7</b>	<b>42.1</b>
<b>Statutory capital utilisation <sup>(2)</sup></b>	<b>73%</b>	<b>70%</b>	<b>72%</b>	<b>76%</b>	<b>79%</b>	<b>81%</b>
<i>SIP2018-20</i>			<i>70%</i>	<i>71%</i>	<i>71%</i>	
<u>Capital adequacy:</u>						
Required capital	11.9	11.2	11.9	12.5	13.1	13.7
Available capital	15.4	16.2	16.5	17.0	17.6	18.3
<b>Capital adequacy utilisation</b>	<b>77%</b>	<b>70%</b>	<b>72%</b>	<b>74%</b>	<b>74%</b>	<b>75%</b>
<i>SIP2018-20</i>			<i>73%</i>	<i>73%</i>	<i>72%</i>	

(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 €30.4 billion at the end of 2018 to €35.2 billion at the end of 2021, an increase of 16%.

- Statutory capital utilisation is projected at 81% by end 2021 reflecting a significant increase in operating assets but still well within the 92% prudential threshold.

- Capital Adequacy Policy ('CAP') utilisation is projected to increase from 72% in 2018 to 75% by end 2021, within the 90% prudential threshold. This compares to 72% CAP utilisation at end 2020 projected in the SIP2018-20.
- Estimates of rating agency capital assessments have been projected for each year of the plan. The Bank remains comfortably above minimum thresholds for triple-A capital strength throughout the SIP2019-21 period.

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 2021 and assuming that the average risk rating for each region remains unchanged, the average capital requirements for debt would be around 21% of debt exposure by end 2021 (Sept 2018: 21.2%).

Overall, it is clear the Bank has appropriate capital to support and implement its plans in the period to 2021, 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<sup>4</sup> and the equity portfolio growth and returns.

Relative to SIP2018-20, the statutory capital utilisation projection in SIP2019-21 is higher mainly due to the projected increase in operating assets (numerator). In terms of income generated from these assets, there is a time lag which impacts the capital base in the denominator of the ratio. In addition, a large proportion of the statutory capital base relates to the amount of callable capital, which is unchanged. The result is the numerator growing at a faster pace than the denominator in the initial years and hence a higher overall statutory capital utilisation compared to the last year's SIP.

In contrast, CAP utilisation is only marginally higher than the projections in SIP2018-20. The growth in required capital (numerator) is lower than that of operating assets as it takes into consideration the risk weighting applied to each exposure.

As noted in the introduction to this section, the financial projections and analysis presented here are based on a planning level of 2019 ABI range of €10.2 billion. If the upper end of the range was achieved - €10.6 billion - the impact on capital and liquidity is expected to be minimal. With regards to capital utilisation, the impact of adding to the stock of assets reflects the interplay between additional capital requirements and the expected increase in income. As a result, capital utilisation would rise marginally to 75% in 2020 and 2021 (2019 planning level: 74% and 75% for 2020 and 2021 respectively). In terms of the liquidity needs set out in section 6.5, again the change is expected to be small with the coverage of the next two years' net cash requirements forecast at 122% for 2019 (2019 planning level: 124% for 2019). Finally, the incremental impact from the Bank's stress test due to this higher ABI result in 2019 is *de minimis*.

## **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. It 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.

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<sup>4</sup> For example, CAP utilisation at end 2021 would increase by around 2% if the Euro depreciated from the \$/€1.15 planning rate to a rate of \$/€1.0

To evaluate the robustness of the plan, the stressed parameters from the Cyclical (1 in 7 years) and Severe stress scenarios (1 in 25 years) within the 2018 Annual Bank Wide Stress Test have been applied to the SIP2019-21 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 consistent with retaining a triple-A rating under rating agency methodologies, whilst relying on perceived shareholder support for such a rating. Under the Bank's Capital Adequacy Policy, this equates to a capital utilisation level of 100% after stress.

The key impacts of the severe stress are:

- 3-year cumulative debt losses of €1.2 billion (base case: €0.45 billion debt losses).
- 3-year cumulative equity fair value decline of 26% or losses of €1.1 billion (base case: 22% growth or €0.9 billion gain).
- 3-year total cumulative debt and equity losses of €2.3 billion.

Based on the severe stress and maintaining planned investment levels outlined in the SIP operational plan, capital utilisation at end 2021 is projected to be at 85%, compared to 72% at end 2018.

**Table 6.3: Capital utilisation results - Severe stress test**

Scenario	Peak Capital Adequacy Utilisation	Increase in Capital Utilisation from YE 2018
Severe with SIP 2019-2021 operational plan	85%	13%

In conclusion, the results from the stress test confirm that the capitalisation levels are very strong and the Bank would remain resilient in the event of a severe shock during the implementation of the SIP2019-21 operational plan.

### 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. 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 and Cyclical stress scenarios 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<sup>5</sup>**

FLTT Metric	Cyclical	Cyclical FLTT	Severe	Severe FLTT
Net Earnings 1 year (€m)	-849	-2,000	-2,374	-3,700
Net Earnings 3 year (€m)	-387	-1,100	-1,361	-3,000
CAP Utilisation 1 year	2%	7%	6%	16%
CAP Utilisation 3 year	4%	10%	13%	18%

The results from these stress scenarios applied to the SIP2019-21 plan are presented below together 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 the Bank's stronger current capital position and by refinements in the methodology to make the scenarios more consistent. One scenario element with significant impact was the assumption of a lower USD to EUR appreciation which is sensitised in this year's SIP given its importance. The SIP2019-21 plan is within all the risk appetite parameters.

As in any theoretical exercise, the actual behaviour of key variables may differ from that assumed, to highlight:

- **USD/EUR exchange rate:** the severe case assumes 5% US dollar appreciation against the Euro. As an illustration, if such an appreciation would reach 30%, and all things remaining the same, capital utilisation would increase by an additional 5 percentage points.
- **Operational assumptions** such as reflows, disbursements, cancellations could behave differently from recent trends.
- Maintaining the **share of equity investments** may prove difficult in a crisis. If new equity transactions were to slow, it would drive a reduction in profits when the market is assumed to recover at the end of the period of stress. This would also result in a reduction in capital requirements.

Nevertheless, the Bank will always preserve the flexibility to adapt investment levels or risk and product mixture to respond to unexpected events.

## 6.4 2019 Financial objectives

### 6.4.1 Financial performance objectives in the scorecard

The Bank's financial performance is assessed within the 2019 corporate scorecard through:

- A targeted return on required capital (RoRC) of at least 3.5% which is assessed on a 3-year rolling average basis to mitigate potential volatility on an annual basis;
- The Bank's realised profit before impairment as a tracked measure; and
- Non-sovereign loan impairment ratio (NPL ratio), which is also a tracked measure.

### 6.4.2 2019 projected income

#### *Return on required capital (RoRC)*

The base case financial reporting profit before net income allocations for 2019 is €660 million (see table 6.5).

<sup>5</sup> The peak capital impact for the Cyclical scenario occurs in year 2 of the stress due to an assumed recovery in equity valuations in the 3<sup>rd</sup> year. For prudence, the 3-year FLTTs have been tested using the financial position at the end of year 2. The Severe scenario FLTTs are tested as normal (peak impact observed in year 3).

**Table 6.5: Projected income for 2019**

€million	Banking activities					Treasury activities	Operational risk	Total
	NS debt	Sovereign	Debt	Equity	Total			
Net interest income	578	53	631		631			631
Fee and commission income	116	29	145		145			145
Net gains from loans at FV and amortised cost	26		26		26			26
Dividend income				103	103			103
Realised and unrealised equity gains/(losses)				234	234			234
Treasury operating income						120		120
<b>Total income</b>	720	82	802	337	1,139	120	0	1,259
Impairment (general and specific)	(163)	(3)	(166)	0	(166)			(166)
<b>Risk adjusted return before costs</b>	<b>557</b>	<b>79</b>	<b>636</b>	<b>337</b>	<b>973</b>	<b>120</b>	<b>0</b>	<b>1,093</b>
Total administrative costs								(433)
<b>Total net profit (before net income allocations)</b>								<b>660</b>
<b>Opening required capital <sup>(1)</sup></b>	<b>5,648</b>	<b>850</b>	<b>6,498</b>	<b>3,793</b>	<b>10,291</b>	<b>1,440</b>	<b>194</b>	<b>11,925</b>
<b>RoRC (before costs)</b>	9.9%	9.3%	9.8%	8.9% <sup>(2)</sup>	9.5%	8.4%		9.2%
<b>RoRC (after full costs)</b>								5.5%

(1) Required capital is based on 2018 forecast.

(2) Return on capital for 2019 is illustrative based on assumed equity return for the year.

Within this:

- Banking is projected to contribute operating income of €1,139 million before provisions, expenses and return on capital and €973 million after impairment.
- Treasury is projected to contribute operating income of €120 million (of which €04 million income from investment activities and €16 million from funding activities) before provisions, expenses and return on capital.

Overall, the 2019 financial plan shows a 5.5% annual return on required capital:

- Debt is planned to contribute around 58% of the total risk adjusted return before costs (€636 million/€1,093 million) with a RoRC return before costs of 9.8%. Within the overall debt return, RoRC before costs for non-sovereign debt is projected at 9.9% in 2019. This is higher than the overall projected return generated from the flow of recent deals - RAROC before costs from debt projects approved by the Board (including those through delegated authority) in the first nine months of 2018 was 8.3% (non-sovereign debt: 8.9%). The assumed 6.5% overall nominal equity return is equivalent to 8.9% of opening required capital, which is slightly lower than the projected debt return before costs.
- Treasury investment returns reflect a conservative investment policy and expanded Treasury activities.

Of the projected total opening required capital at year end 2018, 54% relates to debt, 32% to equity, 12% to Treasury and 2% to operational risk.

The projected RoRC of 5.5% compares to 4.1% estimated for 2018 compared to a 2018 Business Plan figure of 4.4% (See table 6.1).

## 6.5 Liquidity and 2019 borrowing proposal

The assessment of the Bank's liquidity requirements and resulting proposals regarding the size of the Borrowing Programme is made annually in the medium term context provided by each SIP.

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 cash flow 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 proposal, 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 2019 of €9.0 billion net new issuance** is proposed. This proposal includes the approval by Board of Directors on 1 October 2018 to execute pre-funding of the proposed 2019 requirement in 2018 up to an amount of €2.0 billion in order to permit Treasury to take advantage of opportunities offered by the market to secure long-term funding ('Pre-Funding the 2019 Borrowing Programme'). The proposed €9.0 billion Borrowing Programme for 2019 represents a €1.0 billion increase when compared to the €8.0 billion Borrowing Programme in 2018. This planned increase is mainly attributable to higher planned operating cash flows and an increased level of scheduled repayment of borrowings.

To the end of September 2018, €7.2 billion of funding has been raised with an average maturity of 4 years and an after-swap cost of funds of LIBOR less 3.2 basis points.

It is projected that at the end of 2019 the Bank will have 124% coverage of the next **two years' net cash requirements** (to end 2021), as illustrated in table 6.6. These cash flows, including within year, remain volatile.

The projected liquidity levels at the end of 2019 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 meet 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 2019 is projected to be around 107% (end 2018 estimate: 115%; including pre-funding a proportion of the proposed 2019 Borrowing Programme).

**Table 6.6: Projected next two years cash requirement ratio at end 2019**

	Year end 2019	Year end 2020	Year end 2021	Aggregate 2020-2021
<b>€billions</b>				
<b>Opening Gross Treasury liquid assets (excl. pre-funding)</b>	<b>27.8</b>			
Pre-funding of 2019 Borrowing Programme in 2018	1.0			
<b>Sub-total</b>	<b>28.8</b>			
Less: short-term debt	(8.0)			
<b>Opening Net Treasury liquid assets</b>	<b>20.8</b>			
<b>Movements in the year:</b>				
Net operational disbursements and profit, net of net income allocations	(1.3)	(1.1)	(0.7)	(1.8)
Scheduled debt redemptions (incl. new issuance)*	(6.1)	(8.1)	(7.3)	(15.4)
<b>Net annual cash requirements</b>	<b>(7.4)</b>	<b>(9.3)</b>	<b>(8.0)</b>	<b>(17.3)</b>
<b>Projected funding level (€bn less €1bn pre-funding in 2018)</b>	<b>8.0</b>			
<b>Closing Net Treasury liquid assets</b>	<b>21.4</b>			
*Years 2020 and 2021 includes an assumed proportion of new funding yet to be issued. Assumption: 10% of new issuance redeemable within 2 years.				
	<b>End 2019</b>			
Next two years' net cash requirement	17.3			
Net Treasury liquid assets (includes € billion projected funding)	21.4			
<b>2 year net cash requirements coverage ratio (min. requirement 75%)</b>	<b>124%</b>			

The size of the proposed 2019 Borrowing Programme is based on the Liquidity Policy and setting an operating target above the minimum requirements. This continuation of 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 €20.8 billion (including prefunding part of the 2019 Borrowing Programme) estimated for end 2018 to €21.4 billion at end 2019.

**Table 6.7: Projected 1 year EBRD stressed ratio**

	End 2017 Actual	End 2018 Estimate	End 2019 Projected
<b>1 year stressed EBRD ratio (min. requirement 100%)</b>	106%	115%	107%
Headroom above the min. requirement (€billion)	1.3	3.4	1.7

## 7. STRATEGIC PORTFOLIO ASSESSMENT

The SCF emphasises the need to pursue the Bank's transition mandate through a '...balanced and diversified portfolio in terms of geographic, sector and product composition in order to ensure the Bank's financial sustainability...'. The Bank's portfolio also reflects the strategic directions from the SCF in combination with the Bank's core operational principles – transition impact, sound banking and additionality. Naturally, the external context, such as the strength and speed of reforms, as well as the internal context, such as staffing and grant availability, also influence how the portfolio evolves.

The SCF provides geographical direction by putting emphasis on the importance of the Bank's work in countries, and regions of countries, which are less advanced in transition, particularly the Early Transition Countries, the Western Balkans and SEMED. At a product level, there is an expectation that equity – subject to the presence of attractive transition and financial opportunities - will take a more prominent part in the Bank's portfolio.

This section provides an overall assessment of the degree to which the Plan presented in this document matches with the orientations in the SCF, recognising that there is no single, optimal composition of the Bank's activity.

### 7.1 Toward a balanced portfolio

As the SCF makes clear, the objective of pursuing a balanced portfolio is to combine achievement of the Bank's transition mandate and its financial sustainability. Consequently, at the aggregate level the consistency of the Bank's projected portfolio with the SCF objectives is best summarised by its overall size, the expected and ongoing transition impact and its anticipated financial performance.

The projections contained in this document are fully in line with these high level objectives:

- For transition, the Bank's performance management system is designed to deliver ambitious ETI and PTI levels over the period covered by the SIP;
- The operational projections show a growing level of investment activity, portfolio and operating assets supporting increasing transition impact (as described in section 5) and
- The financial projections show rising levels of capital utilisation whilst remaining well within the Bank's capital limits (as described in section 6). The projections also show that average annual capital growth over the SCF period would be almost exactly 4% with the three year rolling average of return on required capital, well above the floor level of 3.5% throughout the period.

In short, the key transition and financial objectives the portfolio implied in this Plan are balanced.

### 7.2 Strategic fit with SCF geographical priorities

With regard to the geographical strategic orientations from the SCF, table 7.1 shows the projected evolution of the Bank's portfolio over the period covered by this SIP by region. The expansion of the portfolio over this period reflects the higher level of ambition set out in section 5 with portfolio growth focused in the SCF priority regions, which is exaggerated for SEMED reflecting the lower relative maturity of the Bank's portfolio in the region.

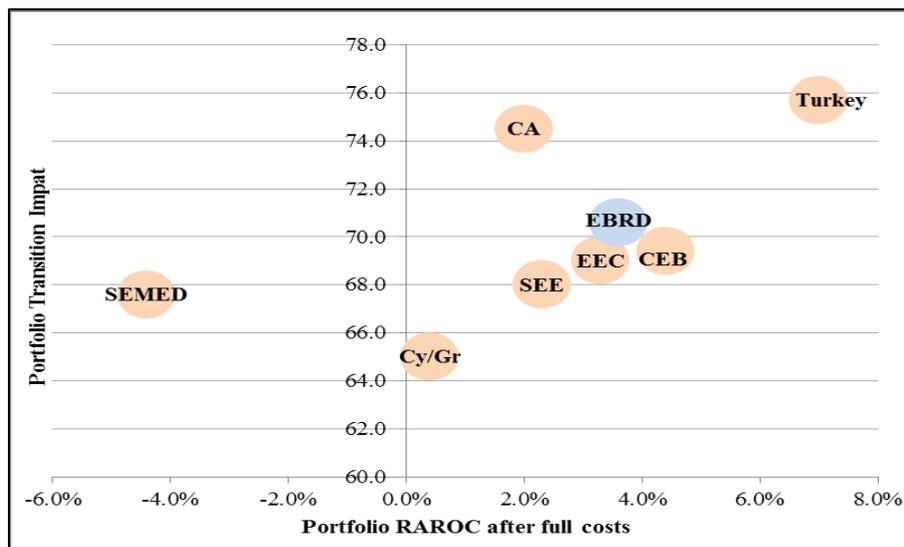
**Table 7.1: Change in portfolio by region 2017 to 2021**

	Change €m	Share of incremental change
Central Asia	+1,200	12%
Central Europe and Baltics	+0	0%
Cyprus and Greece	+800	8%
Eastern Europe and Caucasus	+1,800	18%
South-Eastern Europe	+900	9%
Southern and Eastern Mediterranean	+4,800	48%
Turkey	+500	5%

To help set this evolution in the context of the current portfolio chart 7.1 shows the relationship between transition – measured by PTI – and financial return – measured by portfolio RAROC 2016/17 by region. It shows that within this snapshot of the portfolio:

- **Turkey** is a strong performer on both transition impact and financial returns;
- **Cyprus and Greece** are seeing strengthening transition impact as the portfolio matures with risk adjusted returns just positive, having been strongly negative previously;
- **SEMED** is seeing continuing strengthening in transition performance. Financial returns have improved, but remain negative overall.
- **Central Asia** is strong on transition (especially in the sovereign sector) although below average financially.
- Other regions converge to Bank average on both transition and financial returns, although risk is lower overall in **CEB** than elsewhere.

**Chart 7.1: Transition and financial return by region**



It is important to note that this analysis is backward looking and does not predict future performance. Also, this analysis is critical to understanding the performance of the actual portfolio and usefully informs – but does not determine – the planning process. Many factors, including shareholder priorities and available opportunities, lead to choices about where to invest. An approach which only looked to prioritise investments where transition impact and financial sustainability are optimised would lead to a skewed portfolio, without a link to the Bank’s overall strategy and external events.

This is clearly illustrated by the case of the projections for Turkey, for example. The sharp change in economic expectations over the medium term, together with the more challenging reform environment have led to a more cautious and uncertain assessment of the Bank’s future activity in the country, irrespective of current performance. In addition, some moderation of growth in the stock of assets in the country was to be expected from a risk concentration perspective, in view of its relative size in the Bank’s overall portfolio.

Amongst other regions, transition performance is acceptable across the board. In financial terms, the growth of SEE, CEB and EEC balances the growth of the less financially strong SEMED region. There is some evidence that financial performance is picking up in SEMED in the first half of the year, although the sample size is relatively small. However, both SEMED and Central Asia – where nearly all members are Early Transition Countries – are explicit SCF priorities. The balance presented in the Plan also reflects the approach to graduation highlighted in the SCF that ‘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)'.

### **7.3 Other portfolio features**

Two other dimensions of portfolio balance are worth noting. Reflecting the projected levels of equity activity and anticipated divestment, the equity share of the portfolio is projected to decrease from 18% in 2017 to 15% in 2021. The Bank does not set quantitative equity targets largely to avoid creating pressure to pursue marginal investments to fulfil arbitrary goals and recognises the essentially opportunistic nature of equity investment.

The Agreement Establishing the Bank puts limitations on the Bank's state sector portfolio ratio. However, in terms of the financial balance of the portfolio, it is the sovereign share which is important. Sovereign business commands a fixed margin of 1% over LIBOR whilst all other Bank investment – public or private – carries a commercial rate, with no significant difference in returns between the two. While the sovereign share of ABI is projected to remain broadly constant over the SIP period around 18% reflecting the importance of sovereign lending as a vector of transition impact in some priority regions, the sovereign share of the portfolio is projected to rise from 22% in 2017 to 29% in 2021 due to the longer maturity of sovereign loans relative to other banking products.

## **8. RESOURCING**

This section presents the Bank's resourcing needs to deliver both its objectives over the period covered by the SIP. The focus is on the presentation of the 2019 Administrative Expense Budget proposal with illustrative projections for the remainder of the period to 2021. These projections do not prejudice decisions to be made in future years. Accordingly, the section is structured as follows:

- Section 8.1 explains the motivation behind the construction of the Administrative Expense Budget;
- Section 8.2 shows the composition of the proposed 2019 Administrative Expense Budget and also explains the process through which the budget has been formulated to ensure the efficient use of resources;
- Section 8.3 presents an update on the realised financial results stemming from OE&E programme funded by the separate OE&E Investment Budget;
- Section 8.4 contains the formal proposal for the 2019 Administrative Expense Budget and incremental OE&E Investment Budget;
- Section 8.5 provides an illustrative projection of the evolution of the Bank's Administrative Expense Budget over the entirety of the period covered by this SIP; and
- Section 8.6 outlines the refreshed approach that is being taken to workforce planning and HR management together with information on the composition of the Bank's employees.

### **8.1 Rationale for the proposal**

Over the last two years the Bank's approach to resourcing has been to operate with Administrative Expense Budgets which were no higher than the 2016 level, excluding the impact of compensation related expenses and material strategic changes in the Bank's work. Supported by the recurrent impact of savings from the OE&E programme as well as rigorous prioritisation, this objective has been successfully delivered. Such an approach was appropriate during a period of limited growth of operating assets and portfolio and has been effective in focussing efforts to increase efficiency in the Bank, but cannot be a permanent feature of resource planning in a healthy institution with a significant growth ambition.

Consequently, in the light of the higher level of business ambition in 2019 a moderate increase in the volume of resources is proposed.

The proposed 2019 Administrative Expense Budget shows growth of 2.9% or net zero real increase. Of this, around 2.8% relates to price increases (including 1.3% for the 2019 compensation proposals, a further 0.5% for the proposals stemming from the Bank's Reward Review and the remainder from contractually agreed inflationary increases), with only 0.1% net increase proposed for incremental volume of resources to support business objectives.

This budget will support:

- The ambitious programme of accelerated operational delivery outlined in section 6. Within this, planned operational growth is concentrated in those areas less advanced in transition, including SEMED and Central Asia;
- The accompanying growth in the portfolio and the Bank's operating assets as highlighted in section 5;
- Pursuing opportunities for wider public sector engagement including SOE restructuring and privatisation, together with renewed efforts needed to support project implementation and disbursement given an increased sovereign portfolio;
- Improved quality of the Bank's activity including raising disbursements and screening an increased number of potential equity transactions to increase selectivity;
- Institutional strengthening – such as a reinforced Project Complaint Mechanism – where the Bank is behind peer institutions.

It is also important to recognise that the proposed plan is more resource intensive not only due to the ambition to undertake more activity, but also the changing nature of that work. The projections anticipate a rise in the level of investment undertaken in 'small' countries in which projects tend to be smaller in size and more resource intensive than those in larger economies. There are also trends in the Bank's business which point to rising complexity. For example, preliminary integrity checks have risen at 20% per year over the last two years and half of the Bank's projects have been examined by the Office of the Chief Compliance Officer in the past year against a quarter in previous years.

The proposed budget reflects a rigorous and prudent approach to budgeting, consistent with supporting the Bank's financial sustainability. The administrative expense budget (i.e. excluding the impact of OE&E investment costs) represents 33.5% of projected income for 2019. The income projection represents a prudent view of expected income, notwithstanding that actual results will be volatile in any given year, particularly for equity returns. As such, the proposed budget is consistent with achieving a cost-to-income ratio over the medium term comfortably below the 40% trigger and 50% limit (see section 2).

## **8.2 2019 Administrative Expense Budget**

The proposed Administrative Expense Budget for 2019 is £370.0 million as summarised in table 8.1.

**Table 8.1: Administrative Expense Budget for 2019**

Administrative expenses	2018	2019	2019 vs 2018	
	Budget	Budget	million	%
£m				
Operating expenses	338.6	348.8	10.2	3.0%
Depreciation	20.9	21.2	0.3	1.4%
<b>Admin Expenses GBP</b>	<b>359.5</b>	<b>370.0</b>	<b>10.5</b>	<b>2.9%</b>
GBP/ EUR rate	1.11	1.14		
Admin Expenses EUR	399.0	421.8	22.8	5.7%

Table 8.2 sets out the proposed 2019 budget increases and savings, resulting in an overall Administrative Expenditure growth of 2.9% (5.7% increase in euro terms). Of this, 2.8% budget growth is driven by price increases (including 1.8% for 2019 compensation and reward proposals), while 0.1% budget growth is to fund incremental resources supporting the business objectives. This proposal represents the incremental needs after a serious examination of priorities to optimise the existing budgets by reallocating resources of approximately £7.2 million (or 2.0% of the Bank's budget). These reallocations were enabled by repeating an exercise started last year to right-size budgets and the delivery of incremental OE&E savings.

The conversion of the sterling budget into a euro budget was made at an exchange rate of GBP/EUR 1.14. The volatility resulting from the present political environment in Europe means that this assumption is subject to considerable uncertainty.

**Table 8.2: Summary of 2019 budget increases and savings**

	PROPOSED	SAVING	=	NET REQUEST	
Compensation proposals	4.7		=	4.7	1.3%
Reward proposals	1.7		=	1.7	0.5%
Compensation carry over	1.6		=	1.6	0.4%
<b>Total Compensation and Reward</b>	<b>8.0</b>		=	<b>8.0</b>	<b>2.2%</b>
Other price/ FX factors	2.6	(0.4)	=	2.3	0.6%
Business resources	7.1	(6.8)	=	0.2	0.1%
<b>TOTAL</b>	<b>17.7</b>	<b>(7.2)</b>	=	<b>10.5</b>	<b>2.9%</b>

The composition shown in table 8.2 of the movements in the Administrative Expense Budget is broken down in detail in table 8.3.

Taking each element in turn:

- **Compensation and Reward proposals** (within (a) in table 8.3).
  - **Compensation proposals.** The 2019 Administrative Expense Budget incorporates an increase of £4.7 million based on the proposed staff compensation adjustment and the associated impact on benefits linked to salaries and the performance based compensation pool from 1 April 2019 (the impact for nine months), resulting in a 1.3% budget increase.
  - **2019 Reward Review.** A total of £1.7 million additional budget is included to support structural changes in the staff benefits proposed as a result of the Reward Review exercise in 2019. This factor leads to a 0.5% increase over the approved 2018 Budget.
- **Compensation carry over** ((b) in table 8.3). This factor includes the full year impact of the 2018 Compensation adjustments (see BDS18-008, table A.1).
- **Price and FX movements** ((c) in table 8.3). Within this factor, £2.3 million reflects 0.6% net increases driven by *inflation related impacts and foreign currency movements*. This includes £1.2 million relating to increased medical insurance premiums driven by higher claims, £0.9 million increase of HQ occupancy costs driven by contractual commitments, increases in information services costs as a result of supplier increases. In addition, budget is included to fund assumed compensation adjustments for the Board of Directors, Vice Presidents and other senior staff increases. These increases are partly offset by a reduction in the staff costs budget due to foreign currency movements. Other inflationary impacts have been absorbed within existing budgets.
- **Business needs and other adjustments** ((d) in table 8.3). This factor corresponds to a net increase of the budget by 0.1% for business resources detailed below. Within this:
  - £4.1 million of increases to departmental and centrally managed budgets are **to support the delivery of the Bank's strategic priorities**. The resource increases reflect phased budgets recognising recruitment timelines and have a full year impact of £6.0 million. Proposals were initially for increases of £14.0 million which were assessed, discussed with departments and prioritised. As a result, the strategic areas identified as priorities were: further significant strengthening of the equity function; mainly RO based resources to support growth of business, implementation and protection of assets; incremental resources for Sustainable Infrastructure Advisory (SIA, previously IPPF); supplementary resources working on domiciliation issues; an incremental resource to support local currency activities; additional funding required for the Project Complaint Mechanism and incremental resources for the Human Resources Department to support activities under the People Plan (see section 8.8).

A significant number of requests in various areas were not prioritised for funding. CSG resource requests not immediately linked to income generation or increased operational activities were deprioritised. Some of the other proposals were agreed to be in need of further assessment during 2019, while some resource requests were not considered essential at this time.

**Table 8.3: Detail of key movements in the 2019 Budget**

£ million	2018	Proposed	Saving	2019
<b>2018 Budget</b>	<b>359.5</b>			
<b>a. Compensation and reward proposals:</b>		<b>6.4</b>	-	
2019 Compensation & Benefits (9 months phasing)		4.7		
Reward proposals (9 months phasing)		1.7		
<b>b. Compensation carry over:</b>		<b>1.6</b>	-	
2018 Compensation & Benefits (full year impact)		1.6		
<b>c. Price and FX factors:</b>		<b>2.6</b>	<b>(0.4)</b>	
Medical insurance		1.2		
HQ occupancy (utilities, security, catering & service charges)		0.9		
Information services		0.3		
Board, VP and other salary increases (assumptions)		0.3		
FX movement impact on staff costs			(0.4)	
<b>d. Business needs / other adjustments</b>		<b>7.1</b>	<b>(6.8)</b>	
<b>Activities prioritised for 2019:</b>		<b>4.1</b>	-	
Client Services Group (portfolio, equity and advisory)		2.1		
Risk and Compliance (domiciliation, equity, compliance)		0.7		
Finance (income generation, budget function)		0.5		
HR and Corporate Services (HR & OD)		0.5		
Office of General Counsel (equity, treasury, corp. governance)		0.2		
Other (Office of the Secretary General, Communications)		0.1		
<b>Impact of previous decisions:</b>		<b>2.9</b>	<b>(3.0)</b>	
RO occupancy (Cairo)		0.2		
HQ occupancy (other)		0.2		
RO occupancy (Moscow)			(0.9)	
RO depreciation		0.1		
Annual Meeting costs			(0.3)	
Full year impact of Russia regional and Gaziantep RO closures			(0.2)	
IT Operating Model - savings			(1.6)	
IT Operating Model - reinvestments		2.4		
<b>Other reallocations:</b>		-	<b>(3.9)</b>	
Departmental budget reductions			(2.3)	
Other reductions (centrally managed budgets)			(1.6)	
<b>2019 Budget</b>		<b>17.7</b>	<b>(7.2)</b>	<b>370.0</b>

### 8.3 Resource reallocations

The Administrative Expense Budget for 2019 includes significant reallocations within departmental budgets across the Bank. As discussed above a total of £5.8 million (or 1.6% of the 2018 Budget) budget reductions and reallocations are contributing to the funding of priority investments for 2019. This reflects not only reallocations across the teams within departments, but also net reductions of certain departmental budgets.

As in the past, flexible reallocations of staff and budgets are implemented throughout the year to support operational requirements. Reallocations or adjustments since the beginning of 2018 have included:

- Over 35 staff and position reallocations in Banking resources until September 2018. This included new field based roles and reallocations from HQ mainly to the SEMED and EEC regions (Cairo and Kiev in particular); optimisation of resources based in Cyprus and Greece; reallocations within the SEMED region as well as from Russia to Central Asia; transfers across country and sector teams based on the matrix structure of the department;

and further reallocations at HQ (within the Equity Group and across sector teams). This was associated with reallocation of £1.9 million staff costs budget within the department.

- Consolidation of CSG resources working on engagement with the EU, achieved via reallocations within the approved 2018 Budget (£0.6 million from Banking Department to VP, Policy and Partnerships).
- Set up of a new Gender and Economic Inclusion unit within VP, Policy and Partnerships, reorganising two separate teams supported by £1.1 million budget and resource reallocations from VP, Risk and Compliance.
- Consolidation of back office functions to create the Operations and Service Management group within Finance including £3.2 million budget reallocations from OGC.

A further 19 additional positions or £1.8 million budget reallocations within the Banking Department are already reflected in the 2019 Budget proposal, complementing the requests for new priorities discussed above. These include increased resources dedicated to Infrastructure and Energy portfolio work (senior level roles at HQ and junior resources in ROs) and additional field based positions supporting portfolio activities in Turkey and M&S sector in SEMED region.

The Bank is also reviewing the potential to implement a business partner centre, working with a service provider, as a new operating model for corporate services.

#### **8.4 2019 Administrative Expense Budget by expense line**

Table 8.4 presents the 2019 Administrative Expense Budget by cost line.

*The £9.4 million (3.9%) increase in staff costs reflects:*

- + £1.6 million for the full year impact of the 2018 Compensation and Benefits Proposals;
- + £4.7 million additional budget to support the 2019 Compensation Proposals (9 months phasing);
- + £1.7 million proposed increase for structural changes in staff benefits as an outcome of the 2019 Reward Review (9 months phasing);
- + £0.3 million assumed compensation adjustments for the Board of Directors, President, Vice Presidents and other senior roles;
- + £1.2 million additional budget to address medical insurance price increases;
- + £3.7 million linked to staff cost budget increases to fund incremental (volume) priority investments included for 2019 (e) in Table 8.3);
- Offset by a £3.8 million reduction in staff costs budgets as a result of foreign exchange movements and reviewing the departmental and centrally managed budgets.

**Table 8.4: Administrative Expense Budget for 2019**

Administrative expenses £m	2016	2017	2018	2019	2019	2019
	Actual	Actual	Budget	Budget	£m	%
Salary costs	118.4	121.7	130.0	134.9	4.8	3.7%
Benefits	87.1	89.0	93.7	97.4	3.7	4.0%
Performance Based Compensation	16.5	16.8	14.5	15.5	1.0	6.6%
Other Staff Costs	1.8	1.4	1.5	1.4	(0.1)	(9.1%)
<b>Total Staff Costs</b>	<b>223.9</b>	<b>229.0</b>	<b>239.7</b>	<b>249.1</b>	<b>9.4</b>	<b>3.9%</b>
Consultancy/ Legal	24.3	17.8	16.5	12.5	(4.0)	(24.2%)
Travel/Hospitality	9.6	12.4	12.6	13.0	0.5	3.6%
Other Direct Costs	11.2	12.7	13.3	13.3	0.0	0.0%
<b>Non Staff Costs</b>	<b>45.1</b>	<b>42.8</b>	<b>42.4</b>	<b>38.9</b>	<b>(3.5)</b>	<b>(8.3%)</b>
<b>Direct Costs</b>	<b>269.0</b>	<b>271.9</b>	<b>282.1</b>	<b>288.0</b>	<b>5.9</b>	<b>2.1%</b>
Occupancy Costs	31.3	32.4	32.9	32.9	0.1	0.2%
IT and Telecommunications Costs	13.1	11.6	14.9	19.3	4.3	29.0%
Annual Meeting	1.1	1.3	1.5	1.2	(0.3)	(17.6%)
Central Staff Expenses	5.3	4.7	4.9	5.1	0.2	4.8%
Institutional Fees/ Expenditure	1.4	1.3	2.0	1.9	(0.1)	(4.6%)
Depreciation	20.1	18.8	20.9	21.2	0.3	1.6%
Contingency			0.3	0.3	-	-
<b>Total Centrally Managed costs</b>	<b>72.2</b>	<b>70.1</b>	<b>77.4</b>	<b>82.0</b>	<b>4.6</b>	<b>6.0%</b>
<b>Total Admin expenses GBP</b>	<b>341.2</b>	<b>341.9</b>	<b>359.5</b>	<b>370.0</b>	<b>10.5</b>	<b>2.9%</b>
GBP/EUR rate	1.36	1.17	1.11	1.14		
<b>Total Admin expenses EUR</b>	<b>464.7</b>	<b>400.1</b>	<b>399.0</b>	<b>421.8</b>	<b>22.8</b>	<b>5.7%</b>

The 2019 Budget contains 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 2019 Budget are £1.3 million, or around 0.3% of the total budget. As discussed in section 8.3, £0.9 million of the Management Reserve will only be released on the achievement of procurement savings.

## 8.5 Departmental budgets

The total direct costs budget for 2019 of £288.0 million is broken down by department in Table 8.5.

- CSG direct costs budget increases by £2.1 million. This is a result of £0.9 million full year impact of 2018 compensation increases and £3.2 additional budget phased for 8 months in 2019 to support prioritised areas (mainly, resources for equity, portfolio, SIA and policy, as well as field based roles to support portfolio activities). The increases are partially offset with reductions of the underlying staff and non-staff cost budgets, including due to foreign exchange movements.
- The direct costs budget of Finance is increased to reflect the additional funding to support the 2019 priority areas, namely Treasury activities (income generation, local currency activities) and the Bank's Budget function.
- The reduction of the VP, HR & Corporate Services budget is mainly driven by £3.7 million reductions in IT staff costs and consultancy budgets with increases to centrally managed costs (vendor based service model). The underlying budget, however, also reflects additional £0.4 million budget for the HR and Organisational Development team to fund incremental staff resources (Employee Relations, Talent Acquisition and Development), business analysts and project management support linked to work planned for 2019 (People Plan).

- VP, Risk and Compliance direct costs increase is mainly attributed to priority areas in 2019 (£1.1 million). This includes additional resources for Risk Management (equity) and OCCO (domiciliation, project integrity) supporting incremental activities of CSG, as well as to provide funding for the Project Complaint Mechanism proposal. The increase in priority areas is partially funded by review and adjustment of underlying staff and non-staff cost budgets within the Vice Presidency.
- Office of General Counsel is allocated additional resources mainly to support CSG (equity, portfolio, corporate governance) and Treasury activities. This was funded by £0.3 million adjustment of underlying staff and non-staff cost budgets, resulting in a net reduction of £0.2 million.
- Incremental resources for the Office of the Secretary General to support higher levels of Board activity.
- Additional direct costs budget for Communications reflects an incremental resource for the Business Information Services team linked to increased volumes of integrity checks.

**Table 8.5: Direct costs by department**

<b>Direct Costs £m</b>	<b>2018 Budget</b>	<b>2019 Budget</b>	<b>Variance 18-19</b>
<b><i>Client Services Group</i></b>	<b><i>141.2</i></b>	<b><i>143.3</i></b>	<b><i>2.1</i></b>
Finance	19.3	19.9	0.6
VP, HR and Corporate Service	26.7	23.3	(3.3)
<b><i>Finance and Operations Group</i></b>	<b><i>46.0</i></b>	<b><i>43.2</i></b>	<b><i>(2.7)</i></b>
<b><i>VP, Risk and Compliance Group</i></b>	<b><i>26.5</i></b>	<b><i>26.7</i></b>	<b><i>0.3</i></b>
Office of the General Counsel	16.2	16.0	(0.2)
Office of the Chief Economist	2.3	2.3	(0.0)
Internal Audit	1.1	1.2	0.1
President's Office	1.7	1.8	0.1
Corporate Strategy	1.1	1.1	0.0
Office of the Secretary General	4.2	4.2	0.0
Communications (incl. BIS)	6.8	6.8	(0.0)
<b><i>Central Services Group</i></b>	<b><i>33.5</i></b>	<b><i>33.5</i></b>	<b><i>0.0</i></b>
Evaluation Department	3.1	3.0	(0.0)
Board of Directors	13.1	13.4	0.3
Unallocated	18.9	24.8	5.9
<b>Total Direct Costs</b>	<b>282.1</b>	<b>288.0</b>	<b>5.9</b>

- It should be noted that unallocated budget includes funding for the 2019 Compensation and Reward Review proposals, estimated performance based compensation pool (£23.8 million in aggregate) as well as the Management Reserve of the Bank.

#### **Headquarters and resident office resources**

All capital expenditure is budgeted for and approved through its effect on depreciation. In 2019, this will correspond to £2.0 million capital expenditure for Headquarters and £2.5 million in Resident Offices (ROs).

Key areas for capital expenditure planned for 2019 include:

- Maintenance and repairs of fire alarm systems, electrical installations, generators, kitchen equipment, and office reconfiguration amongst other things at Headquarters.

- The opening of five satellite offices in Agadir (Morocco), Ismailia (Egypt), Thessaloniki (Greece), Andijan (Uzbekistan), Cluj-Napoca (Romania). This is subject to the Board approval (see Annex 1).
- In existing ROs: reduction in size of the Moscow office, relocation of the Ankara office, expansion of the offices in Tunis and Kiev and the replacement of several vehicles.

The Bank's headquarters lease expires in December 2022. Work on the future London location of the Bank's offices is ongoing. Once concluded a proposal will be made for approval by the Board, including any associated capital expenditure budget.

### **IT resources**

As part of the approval of the 2018 Administrative Expense Budget, it was agreed that there would be quarterly detailed reporting on the implementation of the Bank's IT Strategy – Tech 2020. Box 4 sets out the key achievements of the programme to date.

The planned spend on IT capital, reflected in the proposed Administrative Expense Budget 2019 is around £20-22 million, including:

- £9-10 million for 'in-flight' OE&E projects: Project Monarch (an end to end application to manage external banking and project activities including investment, policy and advisory work) and Project Pegasus (replacement Board documentation platform and modernisation of the applications that support meetings of the Board and Executive Management);
- £2.6 million for Windows 10 upgrade (Microsoft);
- £6-7 million for other 'in-flight' and pipeline focused projects to support Tech2020; and
- £2.5 million for business demand led investments.

For pipeline projects, the business case, scope and budgets need to be finalised and approved by Management.

**Box 4: Tech2020**

The Strategic Focus and Priorities of Tech2020:

- Maintaining, rationalising and modernising the technology landscape including the development of our Monarch Banking platform
- Improving our Cyber security
- Building an efficient, cost effective, capable, expert and sustainable mix of internal and partner technology and implementation capabilities
- Better capture, use and analysis of our data
- Continuing focus on flexible and mobile (non-HQ) working
- Improving internal and external collaboration through technology
- Building scalability and flexibility by moving more of operations into the Cloud

A key enabler of Tech2020 is outsourcing. The creation of a series of partners to take on low value work at lower cost also aims to bring additional expertise and capability specific to the Bank's needs and be introduced at an appropriate pace.

Material improvements in the course of 2018 include:

- Strengthening of IT Governance with a clear linkage between the Bank's Management Committee, IT Governance Committee and IT Leadership
- New technologies – such as BlackBerry Works - and new internal capabilities – such as - vendor management, service integration and management, cloud management - are beginning to make a difference and deliver not only efficiencies but also future potential
- Restructuring of the IT team to interact more effectively with the wider business more effectively leading to improved relationships. Increasing focus on pragmatic cyber defences, agile enough to support the Bank's activity but with good provenance (Cyber Essentials Plus)
- Working to bring in new partners to support work across the programme. The contract with a vendor is close to signing for the first phase: Infrastructure & Operations and Networks & Communications. Cyber Monitoring & Support and Secure Operations Centre as a second phase are in the final stages. For Applications Support & Maintenance and Project Support, the aim is to identify both niche partners and a scalable vendor to support applications.

The substantial modernisation programme is targeted to be delivered within an IT budget which by 2020 will remain unchanged from its 2017 level.

**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 2019 is set within a range of 1.6 to 1.8 operations per million pounds (sterling) of operating expenditure.

**8.6 Operational Effectiveness and Efficiency**

The successful implementation of the OE&E programme has been a key enabler of allowing the Bank to do more qualitatively and quantitatively with the same level of resources in recent years. The capacity created has supported investment in resource priorities across the Bank, including the investments needed to implement the Bank's strategic approach to IT (Tech2020).

Table 8.6 sets out updated projections regarding the **medium term savings** generated by the programme:

- Savings within CSG with a recurring full year impact of £9.1 million were made in 2017.
- In IT, £2.4 million of recurrent annual savings were achieved through actions implemented since 2017 and savings of £2.5 million by 2020 are anticipated through the reshaping of the IT capability model through working with vendor partners, to reach cumulative £4.9 million. Aggregate savings are expected to incrementally increase to £5.2 million beyond 2020. This approach will provide enhanced resilience and efficient service provision at a lower cost through the adoption of problem resolution by artificial intelligence (AI), advanced cyber monitoring and automated support. Implementation of this new capability will continue through 2019, including major changes in the workforce

as new partners come on line. IT continues to identify one off savings where possible, especially where new approaches mean planned operating cost increase can be avoided (such as, more efficient support models for new technologies). The adjustment downwards of the size of cumulative savings (previously indicated) is in part the result of increase in user and usage volumes above that which had been anticipated last year. This material change has been absorbed within the existing IT Department budget and the team continue to provide capacity to implement new initiatives, for example experimenting with robotics and AI that will drive forward the technology agenda.

**Table 8.6: OE&E expenditure and saving 2017-20**

£ million	2017	2018	2019	2020	Total
<b>Total programme</b>					
Client Services	(5.7)	(9.1)	(9.1)	(9.1)	(33.0)
IT Operating Model	(3.6)	(3.3)	(4.9)	(4.9)	(16.7)
Procurement Operating Model	(0.4)	(0.6)	(1.5)	(1.5)	(4.0)
<b>Total savings</b>	<b>(9.7)</b>	<b>(13.0)</b>	<b>(15.5)</b>	<b>(15.5)</b>	<b>(53.7)</b>
OE&E Investment	12.9	3.7	10.2		26.8
Net Investment (saving)	3.2	(9.3)	(5.3)	(15.5)	(26.9)
Of which IT:					
Recurrent annual savings	(2.0)	(2.4)	(2.4)	(2.4)	(9.2)
One off savings (2017 / 2018)	(1.6)	(0.2)			(1.8)
Savings from IT transformation		(0.7)	(2.5)	(2.5)	(5.7)
<b>Total IT savings</b>	<b>(3.6)</b>	<b>(3.3)</b>	<b>(4.9)</b>	<b>(4.9)</b>	<b>(14.9)</b>
OE&E Investment	1.8	1.5	4.2		7.5
Net IT Investment (saving)	(1.8)	(1.8)	(0.7)	(4.9)	(9.2)

- Savings with a recurring impact of £0.6 million were achieved within the staffing of the Procurement function across the Bank in 2017. Further incremental savings are targeted from procurement, including implementation of category management reducing the cost of goods and services procured by the Bank. Additional £0.9 million of annual savings are projected from 2019. Whilst Management is fully convinced that significant savings can be achieved through better category management, the precise identification of the target categories and mechanisms through which the savings can be extracted still require some refinement. As a demonstration of such commitment it is proposed that an equivalent amount (£0.9 million) will be frozen from the Management Reserve and can only be used when and if such procurement savings are realised and reflected in reductions of the relevant departmental budgets.

Overall the implementation of the programme will continue to deliver substantial savings and has already paid for itself.

The **investment budget for OE&E** is fully ring fenced and cannot be used for any other purpose, In addition, with the OE&E investment budget there is no fungibility between FTE related investment and the budget for implementation issues, principally programme management. Unused budget is carried forward until the programme is deemed completed by Management and the Board.

The SIP2017-19 originally anticipated £29.3 million of expenditure over the period to 2019. Overall expenditure is now projected at £26.8 million, recognising £1.6 million savings in the

FTE related costs for CSG and £0.9 million lower other implementation costs. The OE&E budget is approved in tranches, with £24.0 million approved in previous SIPs. A proposal is made for £2.8 million funding (£26.8 million cumulative). The implementation of the programme remains subject to risks and as such the projections prudently incorporate full use of remaining FTE related budgets and the programme contingency.

**Table 8.7: OE&E Investment Budget**

£000	Latest projected expenditure			Total 2017-19	Cumulative approved budget	2019 Budget proposal
	2017 Spend	2018 Spend	2019 Spend			
Client Services	8,777	0	0	8,777	8,777	0
IT Operating Model	1,798	1,519	4,191	7,508	7,053	456
Procurement Operating Model	564	165	480	1,209	664	545
Programme management	1,801	1,992	2,512	6,305	4,508	1,798
Contingency <sup>(1)</sup>	0	0	3,000	3,000	3,000	0
<b>Total</b>	<b>12,940</b>	<b>3,677</b>	<b>10,183</b>	<b>26,800</b>	<b>24,000</b>	<b>2,800</b>

## 2019 Budget Proposal

The Board is asked to approve

- An Administrative Expense Budget of £370.0 million (€421.8 million).
- Incremental budget of £2.8 million (€3.2 million) for the implementation of the Operational Effectiveness and Efficiency (OE&E) Programme. This would result in a cumulative OE&E Investment Budget of £26.8 million over 2017-2019, compared to the £29.3 million originally envisaged in the SIP2016-18.

## 8.7 The Medium Term Profile

Table 8.8 includes an illustrative development of total administrative expenses to 2021, based on an illustrative 5% growth in the nominal budget. Future budgets will need to take into account:

- adjustments to reward to ensure that the Bank remains competitive;
- inflation pressures, including in medical costs and information costs that exceed general price inflation; and
- The need to grow resources to support the operational ambitions within the strategic review.

The Bank remains committed to an efficient use of resources and to strict budgetary control and these indications do not prejudice the development of the budget over the medium term.

**Table 8.8: Projected total administrative expense 2019 – 2021**

£m	2018 Budget	2019 Budget	2020 Estimate	2021 Estimate
<b>Administrative Expense Budget GBP</b>	<b>359.5</b>	<b>370.0</b>	<b>388.5</b>	<b>407.9</b>
GBP/ EUR rate	1.11	1.14	1.14	1.14
<b>Admin Expense Budget EUR</b>	<b>399.0</b>	<b>421.8</b>	<b>442.9</b>	<b>465.0</b>
<b>OE&amp;E Investment Budget</b>				
Anticipated expenditure GBP	3.7	10.2		
<b>Total projected expenditure: Administrative Expense Budget + OE&amp;E Investment Budget</b>				
GBP	363.2	380.2	388.5	407.9
EUR	403.1	433.4	442.9	465.0

## 8.8 The Bank's workforce

### 8.8.1 Workforce Overview

Staff are the Bank's most important asset. This section provides an overview of the Bank's workforce and how the Human Resources and Organisational Design (HR&OD) function will support the delivery of the mandate and strategy of the Bank, as well as supporting the people working for it. Table 8.9 summarises the current composition of the workforce and compares it to the figures of the previous year.

**Table 8.9: Composition of Bank staff**

	2016 Q3		2017 Q3		2018 Q3 <sup>1</sup>	
	Headcount <sup>2</sup>	%	Headcount <sup>2</sup>	%	Headcount <sup>2, 3</sup>	%
HQ	1,581	66%	1,631	66%	1,733	66%
RO	802	34%	826	34%	904	34%
Banking	1,332	56%	1,336	54%	1,455	55%
Non-Banking	1,051	44%	1,121	46%	1,182	45%
Regular	1,850	78%	1,868	76%	1,970	75%
Fixed Term Contract	361	15%	425	17%	514	19%
Shore Term Contract	172	7%	164	7%	153	6%
Non OTE (male)	944	40%	967	39%	1,053	40%
Non OTE (female)	844	35%	919	37%	1,030	39%
OTE (male)	92	4%	94	4%	89	3%
OTE (female)	503	21%	477	19%	465	18%

1. Numbers are as at 30 Sept 2018 and as such will reconcile to the numbers in quarterly reporting to the Board.

2. Numbers are for bank staff on regular, fixed term and short term contracts only.

3. On 30 Sept 2018 the bank was engaging 528 CCTs (contractors, consultants and temporary staff who are not paid via the Bank's payroll) and 145 other staff (Board Directors, Interns, Secondments In).

Two changes are particularly noteworthy:

- The increase in the number of staff on Fixed Term Contracts (FTC) from 15% in 2016 to 19% currently and of these 70% are externally funded, up from 65% in 2017; and
- The increase in the number and share of female non overtime eligible staff (non OTE) with the share in the total workforce rising from 35% to 39% in two years, substantially narrowing the gap to the share of male non OTE staff.

### 8.8.2 The People Plan

The delivery of the Bank's mandate depends upon its people. HR&OD has worked with staff to build a 5 year plan to address a number of important people related issues. In the first half of 2018, more than 750 staff from all levels and functions of the Bank were consulted to identify HR issues which needed to be tackled and the expectations of the HR&OD function. From these consultations a comprehensive 5 year plan has been developed for addressing the challenges which were identified and developing the fully functioning HR & OD department necessary to address them and facilitate efficiencies for the Bank.

The key objectives of the People Plan are to:

- Develop an organisation design capability to support management action to optimise the Bank's organisational design to meet its transition goals.
- Provide tools for strategic workforce planning and analytics, to give the practical information necessary to increase resource flexibility, bring greater rigour to planning decisions and reduce resource cost through better matching of people with strategic priorities.
- Provide 'people analytics' to deepen managers understanding of the Bank's talent and help support 'data driven' decisions on hiring and promotion.

- Increase mobility across the Bank to refresh the skills, provide opportunities for growth, and improve the career options of the Bank's top talent, by clearly communicating career paths and improving the management of turnover, performance and talent.
- Continue work on developing a high performance and learning culture underpinned by better quality management and leadership.
- Continue to improve how the Bank can leverage a diverse workforce and inclusive culture to drive productivity and performance by working on the EDGE and Stonewall certification processes, as well as targeted recruitment of underrepresented nationalities.
- Deliver improvements within overall operating costs (KPIs under development) and improve client satisfaction by 'fixing the basics', and increasing the levels of self-service and process automation.

### **8.8.3 Priorities for 2019**

The plan is accompanied by a five-year road map for implementation. HR's 2019 priorities are to:

#### **a) Fix the basics**

- Re-engineer the Joiners, Movers, Leavers (JML) Process to remove unnecessary process steps, fix known problems, increase levels of automation and clarify responsibilities.
- Implement Data Quality Management across the JML Process to measure data quality, identify and fix the root cause of issues, and monitor the impact of corrective action.
- Take action to create awareness of the importance of wellbeing to enable people to feel supported and engaged.

#### **b) Increase levels of self-service & process automation**

- Create an HR Portal to improve the findability and discoverability of HR related information, tools and systems on the intranet.
- Implement a query management solution (ServiceNow) to consistently log prioritise, escalate and track (and subsequently fix the root cause of) queries.

#### **c) Build analytics capability**

- Continue work to create 'usable' HR data that can be presented visually to solve business problems which have a 'people' component.
- Partner with Finance to better link 'people' with people related cost to create deeper insights into EBRD's underlying people related cost drivers.
- Create HR capability to provide insight into 'why' events have happened and pilot the use of predictive analytics to understand 'what may happen'.

#### **d) Build organisational development & workforce planning capabilities**

- Partner with the Executive Committee to identify how to optimise the Bank's organisational design principles to meet its transition goals.
- Support Corporate Strategy by delivering the organisational design modelling requirements for the pre-feasibility study & outcomes of various discussions on the future of development mechanisms.
- Partner with Finance & Corporate Strategy to create the design & 2020 SIP business case for a strategic workforce planning.

**e) Improve management capability & deepen understanding of talent**

- Introduce Talent Managers to facilitate matching & movement of people across HQ and our ROs to improve confidence that the Bank has the right person in the right job at the right time.
- Expand core curriculum to include courses covering the management of change, projects and client relationships to meet business need for specific expert capabilities.

**Annex 1: Satellite offices in Egypt, Greece, Morocco, Romania and Uzbekistan.**

The Bank proposes to establish five satellite offices in Agadir (Morocco), Ismailia (Egypt), Thessaloniki (Greece), Andijan (Uzbekistan), Cluj-Napoca (Romania). Under the by-laws of the Bank the Board of Directors is required to approve the establishment of any Bank office. This annex explains the purpose of these offices.

Each office will become a vital connection point for the EBRD in these cities where currently the interactions with clients can be infrequent due to the distance the nearest Resident Office (RO). Establishing an EBRD presence in each of these cities will be an important progression for the Bank into regions where there is a clear demand and need for advisory and financial services.

The Bank's experience is that satellite offices allow more efficient access to clients and the provision of a better service, especially to SMEs, for whom proximity is important. Satellite offices also help the Bank gather local and regional market knowledge more efficiently, and allow Bank representatives to participate in regional events and meetings increasing relevance and visibility in the regions. Satellite offices are also used by local and HQ bankers and specialists when travelling to the region for due diligence/monitoring visits. It is envisioned that the satellite offices will be used to build a pipeline for the Bank's direct and indirect lending business notably in Agribusiness, P&T, M&S, FI and MEI sectors. The opening of satellite offices also sends a signal to local, regional and national Government officials that the Bank is interested in the economic development of the entire country and not only the capital cities, thus strengthening the reputation of the Bank.

Over the last two years the Bank has been working towards intensifying the linkages between Advice for Small Business (ASB) and banking. Special efforts have been put on developing and expanding existing scalable products through indirect financing of SME under Pillar 1 with an enhanced integration of finance and advisory. Examples include the Women in Business programme – the flagship programme of the Bank being launched in new countries, the Youth Employment programme expected to be piloted by the end-2018, the Trade Ready programme in Serbia and Georgia launched earlier this year. These increasing synergies between the Bank's SME advisory and finance operations are expected to persist and intensify in the future, contributing directly to the Bank's pipeline development for indirect financing (Pillar 1) but also for DFF SME (Pillar 3) and RSF (Pillar 2) activities. For example, the recently launched Blue Ribbon programme is designed to provide comprehensive pre-financing advisory support, tailor made financing and targeted post-investment value-creation support to fast growing SMEs, which have the potential to generate valuable demonstration effects to the rest of the SME population.

With the opening of the satellite office specifically the Bank aims to achieve Key Performance Indicators (KPIs) with regard to number of advisory projects completed, local companies financed and consultants trained for each office. The increased focus on linkages between banking and advisory will help the Bank generate 1-3 banking projects with local SMEs (one of the KPIs) in each of the regions over the next two years.

The on-going expenses and the one-off capital expenditure are to be borne by the Bank. Local staff and associated non-staff costs are to be borne by donors. It is proposed that all five offices are opened over the course of 2019.