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Wise up! European Development Bank red herring masks critique of EIB's external operations

After more than 18 months of dialogue, consultation and much-needed shedding of light on exactly what the European Investment Bank gets up to when it deploys upwards of EUR 9 billion per year outside the European Union, in early March the efforts of the Wise Persons' Panel (WPP) tasked by national governments and the European Parliament to investigate appeared to boil down to whether – and when – a new European Development Bank could come into being.

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The case for cyanide in Bulgaria's gold mines kicked out

In January this year, Canadian mining firm Dundee Precious Metals announced that it was freezing plans on its investment at the Chelopech gold and copper mine in central Bulgaria because of ongoing legal challenges. The Cyanide-free Bulgaria coalition welcomed the news that came after more than five years of problems and controversies surrounding the Canadian investor's plans to introduce cyanide leaching technologies in order to extract gold at the Chelopech mine.

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WISE UP! EUROPEAN DEVELOPMENT BANK RED HERRING MASKS CRITIQUE OF EIB'S EXTERNAL OPERATIONS

That such mulit-lateral institution-building aspirations grabbed the headlines should perhaps have come as little surprise – after all the WPP was headed by a Frenchman, former IMF chief Michel Camdessus.

But beyond the headlines, had the WPP – that included NGO representation from Bankwatch's Manana Kochladze – not lost sight of its basic remit, namely to assess the "relevance, performance ... consistency with the relevant EU external policies and strategies and of the additionality and value-added of European Investment Bank external operations"?

In spite of the weight given to European Development Bank speculation at the WPP report launch, there was ample evidence that the panel had not signed off on a 'dodgy dossier'. In fact, contained in the report's pages, and prior to its release, a considerable amount of development-focused wisdom remained for EU decision-makers to get to grips with when they deliberate on the EIB's development record to date – the kind of analysis that fleshes out the new directions required to get the bank's up to now so-called 'development lending' working for the people it is supposed to serve.

To accompany and hopefully further inform the WPP report, the campaign coalition Counter Balance chose to release a 'shadow report' that assesses the EIB's non-EU lending record since the turn of the century.

Despite bringing some different nuances to the debate, Counter Balance has nevertheless broadly welcomed the extensive analysis that the WPP undertook of EIB lending activities outside the EU, in particular the WPP's willingness to begin to address the developmental impacts of that lending. There are many proposals put forward by the panel that can help European development finance begin to aid genuine development – as well as several that could have the opposite effect.

However, notable among the WPP's conclusions is that "the EIB should increase its development focus". This fundamental point sits alongside other key WPP reform proposals for EIB lending procedures in its non-EU activities, including the need for the EU's bank to:

• "pay particular attention to the promotion of democracy and the rule of law;"
• place "more focus on quality and tangible delivery of EU objectives and less on the volume of financing;"
• "reinforce due diligence on social aspects (including respect for human rights) in its project cycle work;"
• strenghen "staff expertise in sustainable development, human rights, social/gender issues, use of 'pro-development' project indicators;"
• ensure "clear compliance with EU/agreed international standards on environment and social aspects:"
• provide "more extensive and systematic access to project information, and greater involvement of project beneficiaries and local civil society;"

These proposals can be viewed as essential preconditions for the EIB to fulfil its development mandate, and the bank ought to implement the WPP's recommendations in this regard with some urgency. Without them, the EIB is potentially in violation of its legal obligations, which have been recently clarified in both the European Court of Justice and the Treaty of Lisbon.

Yet, the EIB's development obligations could have taken a more central place in the WPP's report. It defines "the role of the EIB outside the EU [as being] to support EU external policies (including enlargement, neighbourhood and development co-operation policies)."

Arguably this definition does not fully reflect the development role placed on the EIB by a European Court of Justice judgment of November 2008, which found the EIB's former mandate invalid, dissolved it, and requires from any new mandate that:

"EIB financing operations should foster the sustainable economic and social development of [developing] countries, and more particularly the most disadvantaged among them; their smooth and gradual integration into the world economy; the campaign against poverty; the general objective of developing and consolidating democracy and the rule of law; the general objective of respecting human rights and fundamental freedoms; as well as compliance with objectives approved by the EU in the context of the UN and other competent international organisations."

The WPP report acknowledges this new remit, but only on page 14, long after it claims the EIB "does not have a pure development mandate", and that it is "primarily focused on investment/ project financing."

This is correct, but only in so far as it covers the EIB's money disbursal within the EU – EIB investments outside of the EU are, however, conditional on other criteria. The WPP report also calls the bank's new external mandate "an explicit request for EIB operations to support EU development co-operation policies." However, this is a legal requirement, especially under the amended Lisbon Treaty, (Art.21(2)(d) to (g)), that states that the EIB's mandate outside the EU "shall have as its primary objective the reduction and, in the long term, the eradication of poverty."

The implications of Lisbon for the EIB ought to be crystal clear: poverty reduction, not corporate interests, must be the focus of all EIB-backed projects which are likely to affect developing countries. In addition, it is important to assess the EIB's external mandate against the various commitments of the EU for aid effectiveness, to measure whether the EIB has a clear proactive lending strategy with regard to development effectiveness and what criteria the EIB uses when assessing the suitability of a non-EU project.

It is in this context that other WPP conclusions regarding the external mandate have to be seen. The WPP's recommendation of "a streamlined EIB mandate with high-level EU objectives for all reasons, for the purpose of establishing coherence with EIB external activities" is valid, as long as those activities serve development. For development to be served – in any real sense – requires: the establishment of no-go sectors like fossil fuels, which are anti-development, polluting and exploitative; investment in cross-sectoral, long-chain projects that take time and money to bear fruit, and; holding companies to account using mechanisms like benefits for local communities covenanted into project contracts.

Controversially, the sectors or themes that the WPP suggests focusing on do not inspire confidence that development via the EIB can be duly delivered. One is energy security: the EIB is being wheeled out by the European Commission in a massive push to secure EU energy imports, a push – or grab – that involves oil and gas pipelines, solar projects and even a 6,000 kilometre long electricity cable from the Congo River, that has huge implications for geopolitics, regional stability, energy consumption and climate change. These are issues that need to be debated democratically and at length – they should not be automatically allotted vast sums of public money in obscurity.

Another area is climate change. Among policy makers and project financiers there is a deeply worrying trend not to see climate change as an unarguable rebuttal of high-consumption western lifestyles, but instead as a possible source of profit. Carbon trading, offsetting and mitigation and adaptation techno-fixes like 'carbon capture and sequestration' are potential goldmines for corporations; they also actively disguise the only real solution to climate change, which is to reduce consumption.

Counter Balance's own shadow report, 'Corporate Welfare and Development Deceptions,' paralleling the WPP findings, suggests that: "the EIB should stay out of adaptation funding." It further clarifies that: "Regarding mitigation actions, the EIB should prioritise support within the EU, which remains a major emitter compared with neighbouring countries."

Beyond development delusions

The lessons to be learned from the EIB's non-EU lending to date are numerous, and revolve around one fundamental premise that the Counter Balance shadow report foregrounds: people living in poverty are failing to receive the benefit of billions of euros loaned each year by the EIB outside the EU. When the main trends of the EIB's investments are considered, it's not difficult to see why this should be the case.

The EIB has tended to support western mega-corporations at the expense of local companies or needs. In Zambia, for example, three quarters of EIB investments in the period 2005-08 went to the mining sector, which is not even listed among the five priority sectors in the Country Strategy Plan. These investments have precipitated terrible contracts like the one for the Mopani copper mine, in which the Zambian government received an embarrassing 0.7 percent of revenues. The EIB also has a pronounced bias against truly poor countries which need investment most. To its credit, the WPP report details how Asia and Latin America Low Income Countries received a paltry 1.4 percent of EIB non-EU funding in the 2000-09 period.

In short, Counter Balance's 'Corporate Welfare and Development Deceptions' report notes among other failings that:

• "the EIB does not select its projects according to how it can best use public money to maximise poverty reduction and environmental protection for those who need it most;"
• "the EIB does not have a clear understanding of development effectiveness or of the specific contribution it can make;"
• "the EIB's guarantees and grants are mainly used to support private sector operations with little social or environmental value-added;"
• "the EIB should remove the harsh emphasis on cost recovery and instead embrace broader social and environmental goals;"

In other words, and considering its newly clarified development obligations, the EIB is not an institution that should be allowed to continue lending as it currently operates. Major and fundamental changes are required – and quickly, given that the EIB plans to expand its loan volume by 30 percent in 2010 and 15 percent in 2011, on top of a 30 percent expansion last year.

For this reason, the WPP's repeated praise for the EIB's "lean business model" is a source of major concern. It hardly sits well with some of the panel's own conclusions, for example that:

(i) [EIB's] translation of EU policies into EIB lending strategies and the economic and sector analysis of country needs are very limited;
(ii) the EIB efforts to monitor project implementation, ensure local presence and follow up on environmental and social aspects appear still insufficient;
(iii) the EIB ability to satisfy the mandate requirements on development aspects is only indirect.

These conclusions, not to mention the fact that the EIB lends "more than EUR 40 million per staff member, compared with about EUR 3-7 million for a typical MDB [multilateral development bank]," suggest not only that the EIB is understaffed, but that its appraisal, evaluation and monitoring procedures are woefully underpowered and cursory.

The main reason why the EIB is able to operate a 'lean business model' is that despite its improved intentions, it is not set up to do development work. Alone among MDBs, it lacks mandatory project criteria; it selects projects overwhelmingly on economic rate of return criteria; once a project enters the funding pipeline, it is more or less guaranteed support; its monitoring of projects after funding is almost non-existent; it lacks not only staff expertise in evaluating social and environmental pros and cons, but also a fundamental development orientation.

This latter point is the hardest to resolve: it would involve a sea change in institutional culture. The EIB got its development role essentially by default, chifely because the EU wanted to make further investments overseas, largely to serve its own interests, and could not find a more appropriate vehicle to do so. But it is becoming clearer all the time that the EIB is not like other MDBs: it has a legal and political obligation to serve development and in the process to be accountable to the citizens and elected bodies of the EU, something that the World Bank, for example, simply does not have to do.

Bringing in new staff will not be enough to make the EIB serve development. And until it can, as it is legally required to do, the fundamental question should be whether the bank is entitled to carry out development projects at all, not whether to further expand its remit – via increased capital or the tentative talk about its morphing into a European Development Bank.

In this context, WPP suggestions such as the EIB taking on concessional financing, blending grants and loans or increasing own-lending risk are beside the point: in its current form, the EIB is not qualified to promote genuine development, and until those institutional deficiencies are corrected, new approaches will founder.

All the same, several recommendations contained in the WPP report as regards the functioning of the EIB are worthy of mention and further attention:

• "Leverage with borrowers and stakeholders should be used to obtain timely and relevant information on the progress of projects. Disbursements should be closely linked to achievement of project implementation milestones." This latter idea is excellent, and can be taken further, as per a Counter Balance proposal, first expressed in the report 'Conrad's Nightmare' on the proposed Grand Inga dam in the Democratic Republic of Congo, of covenanting specific project benefits into project contracts, with the option of recalling loans if those tangible developmental goals are not met.
• "Monitoring of global loans or loans for SMEs should be improved, to ensure the financial intermediaries properly implement the EIB requirements, to ensure accountability, transparency and environmental sustainability in the use of funds." Of course, these 'EIB requirements' will have to be heavily beefed up for this to mean anything.
• "Indicators and benchmarks to better track the value added and impact of EIB operations should be clearly defined for all regions and sectors, building on the existing ESIAF and including the new development co-operation objectives, and properly monitored throughout the project cycle until ex-post evaluation. In particular, this includes assessment and tracking of the 'consistency with and support to EU policy objectives' (which should now be taken to include development objectives), as well as with specific mandate requirements."

Also providing some positive, concrete signposts for the development journey to come are the criteria that the WPP seeks to apply to a European development institution, notably to:

• "reinforce links and ownership process with beneficiaries;"
• "be fully accountable as a public institution, and focus on tangible benefits and positive impacts for the final project beneficiaries; strengthen the consultation process with local civil society;"
• "improve access to development expertise."

It is questionable, however, how much any of these things will be achieved by a new mega-bank wholly owned and run by European interests.

If what we seek is country-led, pro-poor, sustainable development that is sensitive to the needs of local communities, it remains profoundly unlikely that such goals will be served by a bigger, more unwieldy, top-down mega-bureaucracy. How many good examples of big western bureaucracies serving real local needs half a world away can you find?

The point remains, though, that the criteria the WPP suggests must be the pre-requisite for development lending, especially under the new Treaty of Lisbon. There are minimum conditions that the EIB or any European development arm must meet. Without them, development lending cannot and should not go ahead, regardless of the financial or strategic benefits. It is incumbent on EU institutions, member states and civil society to codify and enforce those conditions.

Essentially, the risk persists that the development question has been posed the wrong way, as exemplified by the issue of what to do with the optional mandate for the EIB of an additional EUR 2 billion. The point is not to find somewhere profitable to put that money. The point is that the EU must first and foremost "do no harm", and as part of that it must ensure that development money serves real development. If it doesn't, it should not be used, regardless of EU, corporate or member state self-interest.

To reiterate, that means a list of no-go areas: no money for fossil fuels or the extractive industries, for instance. It means a fundamental revamp of the EIB to promote long-term, cross-sectoral projects that need time and investment. If the EIB is not capable of that, as we believe it currently is not, then the bank should not be entrusted with an optional mandate to dig more development disappointments and disgraces.

The Counter Balance report Corporate Welfare and Development Deceptions is available at: http://tinyurl.com/3ahqbn6

Lost in transition

During the financial and economic crises we've become so accustomed to banks receiving billions of taxpayer infusions with few conditions attached that, for a lot of people, it may seem unsurprising that the European Bank for Reconstruction and Development is looking for an extra 10 billion euros in capital to expand its investments in central and eastern Europe.

The EBRD is, however, not your average bank, but a multilateral development bank, one with the unique mission of fostering transition towards open market-oriented economies and acting as a catalyst of private enterprise in CEE, investing in projects where financing would not otherwise be available. This request for additional capital from its shareholders - including the EU states, the USA, and Japan - is therefore not a bailout but is supposed to deepen the EBRD's promotion of transition in our region and build on the nearly eight billion euros that the EBRD lent in the region last year.

What is now clearer than two decades ago when the bank was founded, however, is that market economies alone are not enough to meet the social and environmental challenges of the 21st century. The EBRD's own Life in Transition survey in 2007 included the alarming finding among 29,000 respondents across the region that trust in society had plummeted since 1989. While many communist-era environmental nightmares have been ameliorated, the transition countries are driving - at hyper speed - unsustainable trends of rising road transport and waste production, coupled with an enduring legacy of wasteful energy production and consumption. With Russia the fourth largest global greenhouse gas emitter, and countries such as Azerbaijan, Kazakhstan, Ukraine, and Uzbekistan among the world's most energy-intensive, action urgently needs to be stepped up.

Yet the EBRD's new strategic overview for 2011-2015 provides too few answers to these challenges and too much business as usual to justify its requested capital increase. The strategy does aim to support transition to an energy-efficient, low carbon economy, but it is hard to imagine - given the scale of change needed and the inevitable time that this would take - how promoting a low-carbon economy can be reconciled with projects to expand, extend the life of, or even build new coal power stations, not to mention expanding airports, building new motorways, and building oil and gas pipelines.

Yet this is exactly what the EBRD is planning to do, with projects like new coal power plants in Kazakhstan and the Nabucco gas pipeline - with a capacity of up to 31 billion cubic meters per year and a price tag nearing eight billion euros.

Instead of investing in such projects, the EBRD needs to prioritise the use of scarce public financing to lead new markets in new renewables and energy efficiency investments and phase out support for fossil fuel investments, particularly given the larger scale of fossil fuel investments and the likelihood that they will crowd out new renewables financing.

The EBRD's new priorities also talk of support for the corporate sector to support economic diversification and competitiveness. But corporate sector projects are another area in which project selection and appraisal needs to be tightened up if the EBRD is to avoid repeating earlier mistakes, like its series of loans to steel giant ArcelorMittal for environmental improvements, totalling just over 550 million euros over the last ten years, which has brought few visible results as local communities continue to breath choking pollution and raises the question whether the world's largest steel company could not have accessed financing from other sources.

Another important direction for EBRD lending will be support for the private sector by financing micro-, small- and medium-enterprises through financial intermediaries (FI). International development lending channelled through FI like commercial banks or private equity funds has long been a concern for civil society organisations though, particularly because of the glaring lack of control placed on such institutions by the likes of the EBRD or the European Investment Bank when they on-lend to high street banks like Unicredit or Raifeissen. Next to nothing is known about where this money ends up let alone if it is supporting projects that lead to social and environmental well-being.

With the EBRD's FI portfolio now mushrooming to nearly 40 percent of its annual portfolio, the bank needs to provide more assurance – and, ideally, proof – that this money is actually reaching its intended targets and ob-

jectives, like providing start-up capital for cash-strapped small business owners across the region, as opposed to being horded by western commercial banks shoring up their balance sheets or using this finance to leverage larger investments elsewhere.

2009 was a year when huge amounts of public money were poured into black holes in the name of tackling the financial and economic crises, but it was also the year when it was realised that financial activities need to be much more tightly scrutinised and regulated.

2010 must be the year when concrete steps are taken to make this a reality, combining the lessons of the financial crisis with the imperatives of creating a low-carbon, socially just society. The EBRD's shareholder countries now have a prime opportunity to do just that, if only they will seize it instead of handing the bank a blank cheque.

This is an edited version of an article that was published by Bankwatch in Transitions Online (www.tol.org) on March 23 this year.

A Bankwatch briefing paper on the EBRD's Capital resources review 4 is available in pdf at: http://bankwatch.org/documents/SomeWaysForwardForTheEBRD.pdf

THE CASE FOR CYANIDE IN BULGARIA'S GOLD MINES KICKED OUT

Subsequent to this, a conclusive verdict from the Supreme Administrative Court of Bulgaria was announced earlier this month cancelling Dundee's environmental permit for cyanide technology introduction at Chelopech.

Dundee had been expected to apply for project finance from the European Bank for Reconstruction and Development (EBRD) for the cyanide scheme at Chelopech following earlier EBRD loans totalling USD 25 million for operations at the mine.

To mark the tenth anniversary of the Baia Mare cyanide spill, on 11 February a round table discussion on the theme "Cyanide technology – risks and alternatives" took place in Sofia. The event was organised by the Cyanide-free Bulgaria Coalition and Bankwatch member group Center for Environmental Information and Education. The Ministry of Environment and Waters and Chelopech Mining were both invited to this open debate, but declined to participate, although representatives of the Ministry of Health did choose to take part.

This article was presented at the round table. Its author, Dimitar Sabev, is an economist and journalist.

What drives gold mining?

When analysing the dynamics of the gold price since 1970, namely since the abandonment of the idea of the gold standard, a sharp rise in the price of gold after 2002 is noticeable. A similar, though lesser, growth was noted in the early 1980s, followed by a long period of lower prices.

It is to be expected that the price of gold will drop again once the global economy starts to recover from the current recession. In fact it is possible that the price of gold is presently at its peak. But with rising gold prices, what we tend to see is a growth of investments in gold mining – recently the media has even spoken of a "new gold rush". As part of this, in terms of investment cyanide leaching is the cheapest technology – certainly if the assessment excludes the associated health risks and environmental pollution. Cyanide technology secures a good profit from the extraction of gold from poor ores, as is the case with the Chelopech mine.

However, if the price of gold falls in the future, in all likelihood commitments to high standards of operation and subsequent recultivation of mining sites will be abandoned for being unprofitable.

This scenario should not be overlooked in the case of Chelopech Mining. The company insists that it applies the leading technologies with impeccable systems for protection. However, if the price of gold fell below the levels that provide the expected rate of profit, then the company's expenses for environmental and social programs in the region would be likely to decrease as well. Indeed, this tendency has already been seen in the operations of Dundee Precious Metals in Kapan, Armenia, where the company halted its compensation plan in 2008 due to the economic crisis and a temporary dip in the prices of metals.

Who pays for the damage caused by cyanide pollution?

Ten years ago, the Australian company Esmeralda Exploration that was unable to prevent the cyanide spill from the Romanian mine Aurul in Baia Mare described as "politically motivated" all reports that talked about the poisoning of the Tisza and Danube rivers. Australian businessmen claimed that in fact they had introduced environmental standards in backward Romania – indeed, according to the Australians, the reactions to the spill in Hungary and Serbia were "emotional" and "entirely speculative".

The cost of the damage caused by the Baia Mare cyanide spill told a different story, though: it was estimated at 110 million euros. And when the Australian company could no longer reject the obvious, in order to avoid claims for nearly 100 million dollars, Esmeralda Exploration withdrew from the stock exchange in 2002. It was renamed as Eurogold and split from the operator of the Aurul mine (Transgold), ultimately leaving Romanian taxpayers to pay compensation to Hungary.

The same model – environmental disaster followed by a bankruptcy to avoid payment of compensation – prompted a cyanide ban in Montana, USA. The state of Montana is a major centre of the US mining industry. However, poor regulation of mining technologies has lead to a sharp degradation in environmental quality, causing knock-on effects that have degraded the value of other assets such as forests, farmland and tourist sites. Taxpayers have been forced to pay huge bills for rehabilitation and recultivation because mining companies rushed to go bankrupt or changed ownership every time a claim was forthcoming.

According to publicly released information, Chelopech Mining has deposited 2.3 million dollars in a trust account for "financing activities for reduction of environmental risk" – this kind of sum is not sufficient though to cover a serious accident. According to the latest financial statement of the Canadian company Dundee Precious Metals (the concessionaire of the Chelopech mine), net sales for 2008 amounted to 109 million dollars, with total assets valued at USD 568 million. The company's available resources would also be insufficient to offset an environmental disaster that the application of cyanide technology could cause.

Would a ban on cyanide technology impede the economic initiative?

Alternative modern methods for gold extraction, such as the Haber Gold Process, do exist, but the gold industry prefers not to give them publicity, since the marginal costs involved are higher and consequently profits are lower. This is how journalists from the BBC described the accident in Baia Mare: "The spill of cyanide, although devastating, is not the main problem. The wider question is how this situation could ever happen: this is a history of inadequately regulated capitalism in post-communist Romania." (May 19, 2000)

At the same time the cyanide process is not a labour-intensive process. Tripling the production capacity of the Chelopech mine or the development of the Ada Tepe deposit near Krumovgrad, which Dundee Precious Metals is now striving for, is not expected to create many new jobs. Moreover, any jobs created are not such that can bring about a valuable increase in the global competitiveness of the Bulgarian economy. It should also be noted that the expansion of the production process will lead to faster depletion of reserves in the deposit, and therefore the positive social impact of the investment will quickly blow over.

According to today's rates and information made public by the investor, the Chelopech deposits are valued at a total of 4.5 billion dollars, comprising 2.675 billion dollars in gold and 1.9 billion dollars in copper. Under the current concession terms, by 2020 the Bulgarian state stands to gain only about 300 million Bulgarian leva, or just over 200 million dollars. In this case Bulgaria is clearly in a losing position in terms of managing its national resources.

At the same time, though, the risk associated with the introduction of cyanide leaching in gold mining directly affects the ability of Bulgaria to develop the following sustainable sectors:

- Organic farming, viticulture and fruit;
- Environmental and recreational tourism;
- Food-processing industry, especially export opportunities for the European market;
- Fisheries and water resources.

This last one is especially important, since Bulgaria is in the group of countries that are at high risk of droughts. The contamination of groundwater from cyanide tailings – a very definite risk – becomes even more expensive in view of the emerging shortage of water for irrigation and drinking purposes. At the same time, extreme weather events, including floods, have started to become more frequent in recent decades, and this also increases the risk associated with the safe storage of waste products from the cyanide process.

In sum, the introduction of cyanide leaching in gold mining in Bulgaria will fit the unfortunately all too familiar scenario of nationalisation of environmental risk and privatisation of revenues. Furthermore, the environmental risk is an international, trans-boundary one, since the countries of the Aegean basin will not be slow to raise accusations against Bulgaria in the case of a spill.

An analysis prepared by the Market Economy Institute for Dundee Precious Metals states: "[Thanks to the realisation of the gold extraction project in Krumovgrad] the municipality will become a more attractive and preferred place to live." This way of presenting the use of cyanide in an ecologically preserved area, one that has the potential to develop agricultural production with high added value, as well as ecological and cultural tourism, is simply arrogant.

From the perspective of Bulgaria's investment image, it is high time to break up the stereotype of a "country in Eastern Europe, where environmental standards are not an obstacle to doing business." The short-term chance to make gains higher than the average for the industry thanks to controversial technologies, promoted with vague arguments by individual investors, in fact ends up chasing away investors who would be likely to transfer innovative technologies and help improve the overall quality of governance.

New EU funds report and website

A new analysis from CEE Bankwatch Network and Friends of the Earth Europe points to alarming shortcomings in how billions of EU funds earmarked for clean energy projects in the new member states of central and eastern Europe are being deployed.

"Potential unfulfilled: EU funding and Cohesion policy can do more for sustainable climate and energy development in central and eastern Europe" calls for big increases in the marginal allocations that the new member states have thus far given to clean energy schemes, citing widespread evidence from the ground that among other necessary low-carbon initiiatives building efficiency schemes are ready to take off if they become more affordable and if EU money is better targeted.

Bankwatch and Friends of the Earth Europe have worked together over the last decade to ensure more sustainable use of EU funds in central and eastern Europe, in this time compiling a range of ground-breaking analyses that have raised the alarm about ineffective, non-sustainable use of EU money in the region.

The report is available in pdf at: http://bankwatch.org/documents/potentialunfulfilled.pdf

Sustainable EU Funds is a new Bankwatch web initiative that provides a campaign support centre for NGOs from across Europe that are working to ensure sustainable use of the EU Funds.

www.sustainableeufunds.org

EU funds sinking in Latvia's enduring crisis swamp

In February this year Latvia signed new memoranda of understanding with both the IMF and the EU that allow the crisis-crippled Baltic state to continue borrowing from these institutions. While the country's macro-economic situation is now seen as stable, the major challenge is to keep the budget deficit under the ceiling of 8.5 percent that Latvia has pledged to the IMF. Drastic cuts in budget expenditures, accompanied by an increase in tax levels and some structural reforms, have already been agreed upon during budget negotiations for 2010.

However, there are additional expenditures from the budget being made in 2010 after the constitutional court reversed the government decision from July 2009 on cutting state pensions by 10 percent. Thus pensions will be paid in full along with compensation for losses incurred by pensioners in 2009. Further cuts will still be needed in the budget for 2011.

Not surprisingly social tension in the country is rising. The unemployment rate has hit 22.8 percent, the highest in the EU, and is showing no sign of dropping. There is also public fear that mechanical budget cuts to meet the demands of international donors may prove to be counterproductive, bringing only short term fiscal benefits.

Within this less than encouraging climate, both government officials and the IMF have repeatedly stressed the need to use EU funds more actively to promote economic activity. To help with this several bureaucratic administration requirements have been lifted – but in practice EU funds spending is also being negatively affected by the cuts in budget expenditures.

Latvia has reduced the co-financing rate from the state budget to the EU funds programmes thus reducing the actually available public money for programmed activities. Whereas previously one million euros allocated for a new wastewater treatment plan would have involved 850,000 euros from EU money and 150,000 euros from the Latvian government, now and following the reduction in the required co-financing rate, those 850,000 EU euros remain but, with the state looking to make any cuts it can, the other 150,000 has gone.

The impact of this is being keenly felt by pro-environment projects in Latvia – some of the activities financed from the EU funds aimed at nature protection have been substantially cut if they weren't merged in 2009 already. And, for the reasons outlined above, programmes aimed at building and upgrading wastewater treatment facilities in Latvian municipalities – involving measures needed to fulfil the requirements of EU directives on wastewater quality – will be reduced.

Latvia's Ministry of Environment has been arguing that investments into environmental infrastructure also bring economic value-added and the ministry has even been turning to environmental NGOs asking them to help defend its position and to emphasise the need for upgrading environmental infrastructure.

Latvia's environmental NGOs have welcomed EU funds spending for energy efficiency measures – funding is available for heat insulation measures in multi-apartment residential buildings covering up to 50-60 percent of the cost in the form of grants, with the remainder to be financed by apartment owners themselves.

These are regarded as attractive conditions, however the implementation of the programme is not going smoothly. Despite several rounds of applications most of the financing remains untapped. Apartment owners it appears are reluctant to cooperate and moreover are hesitant to take loans to cover the upfront investment costs and their share of investment.

The credit crunch and economic crisis in Latvia are weighing heavily on people's minds, and are clearly setting off warning signs when it comes to the idea of taking out more loans, even for positive initiatives such as domestic energy efficiency.

Charge of the electricity brigade against villagers in Ukraine

On a wet and freezing morning last November, a dozen or so villagers in Usatove, near Odessa in Ukraine, were trying to warm themselves by a small camp fire in the middle of village. At dawn more of their neighbours and acquaintances started joining them, men and women, teenagers and pensioners alike. Anxious but resolute, they quietly talked to each other, their exchanges full of words like 'police', 'storm', 'governor's order' and 'paramilitary forces'.

Not much time elapsed before their fears were realised. "Oh my God!" someone gasped, noticing the imminent arrival of a long caravan of buses, cars and trucks led by a police car through a narrow countryside road.

Policemen arrived in a string of buses and surrounded the villagers keeping vigil by the fire. They were followed by people dressed in orange work vests who brought sections of mobile fences. A police marshal read out a court order obliging Usatove citizens to leave the site. Another two circles of police surrounded villagers and then the attack began. People were forced into a small group and pushed out of the site. A few old women fell down – hard army boots stepped on them and police officers the age of their grandsons pulled them away. After the area was free of villagers, the 'orange vests' immediately erected fences and two lines of police, shoulder to shoulder, began guarding the area.

This is not a scene from the latest big budget crime blockbuster, nor is it a report about a police training exercise. These events took place on the construction site of an EBRD backed project in Ukraine.

These grim scenes were the culmination of the state-owned electricity company Ukrenergo continuing construction of a high voltage transmission line through the village of Usatove, in spite of the original project design routing the line outside the village.

When the project was approved for EBRD financing in 2005, everything looked perfect: the project sponsor Ukrenergo conducted an environmental assessment and consultations with the affected public in line with the EBRD's requirements, the project was viewed as vital for improving the efficiency of the grid in the Odessa region and for providing stability in the electricity supply to Odessa. EBRD staff also deemed the project to have a positive transition impact.

Yet, in the intervening period, things changed. Despite claiming a high importance for the new transmission line, Ukrenergo delayed the start of the construction by almost three years, with the expected date of the project completion by May 31, 2009 not being realised. Ukrenergo also failed to ensure land acquisition for the section bypassing two villages, and therefore opted for the easiest looking solution – running the power lines via a corridor of existing transmission lines through the villages of Usatove and Nerubayske.

Meanwhile a new deadline had been set – December 2009. Several reasons probably accounted for this new choice of date: state budget allocations had to be spent by the end of the year, December 22 is a professional holiday for the Ukrainian energy industry, etc. However the most important factor behind getting things done by December was the presidential elections in January 2010 – and the ruling government was in dire need of making visible achievements to show to voters. However, in this case, the intended effect boomeranged.

Two overhead transmission lines were built through the villages far back in the communist 1960s and further upgraded from 110 kV to 330 kV in the eighties. At that time the authorities paid scant attention to the interests of ordinary people, so the lines literally became 'overhead' for villagers: many plots of land and some homes were situated in the sanitary zone and high voltage came bursting into everyday life.

So when in September 2009 Ukrenergo dismantled the poles of one of the two lines and started installing new towers designed to carry two circuits instead of one, people's patience snapped. Indeed, for more than two months prior Usatove's villagers had effectively blocked construction activities both on site and in the local court. They soon learned about the EBRD's financing of the project and raised their concerns to the bank's Environmental and social department.

The EBRD's reaction was reasonably quick and strong: a site visit was made by EBRD representatives, followed by a clear public demand to Ukrenergo "to halt immediately further construction work and to take measures aimed at defusing the tense situation in the area".

However, even the possibility of being involved in international scandal as well as the threat of further financing being suspended did not prevent Ukrenergo charging on in its rush to complete construction by the end of 2009. Thus, starting on November 16, with back up support from a small army of police, the company resumed installing the new towers in Usatove. As luck would have it, though, nature came to the rescue of the villagers this time – extreme weather conditions significantly hampered the construction activities and the expected deadline was not met in December.

The current situation is unclear. The EBRD has required Ukrenergo to adhere to the initial project design, while at the same time prompting the company "to address possible adverse impacts of the modifications to the original project and to compensate affected parties for the anticipated works".

Seeing the backdoor being opened slightly, Ukrenergo has cooked an amendment to the project's environmental impact assessment and a consultant's survey on the possible electromagnetic impact of the new lines. Although the survey concludes with the clear recommendation to remove the lines from the village boundaries as the best solution, this action is so far not in the plans. Another highly charged rush, then, may well be lined up for the second half of 2010.

Will the World Bank be rewarded for business as usual or put to the test to stop climate-damaging development?

The multilateral development banks (MDBs) are currently requesting a General Capital Increase (GCI) from donor country governments. For the World Bank Group, the IBRD, which lends to middle-income countries, is requesting a 30 percent increase and the IFC, which lends to the private sector, has asked for a 75 percent increase. As would be expected, donors do not typically hand over additional funding without attaching strings, such as key reforms at the institutions in exchange for money.

Given that many donor governments have positioned climate change as one of their top international aid priorities, the question is, will the GCI strings be attached to halt the large-scale financing of fossil fuel development at the World Bank?

The United States appears to be signaling that it is considering this approach, at least with respect to coal. In December 2009, the U.S. Treasury released a note, which was subsequently delivered to World Bank president Robert Zoellick, titled "Guidance to MDBs for Engaging with Developing Countries on Coal-Fired Power Generation." It sets out how U.S. representatives to the MDBs should evaluate proposed coal projects and is intended to encourage "no or low-carbon" energy options prior to selection of coal-based projects.

However, this unilateral move by the US was not appreciated by several Bank executive directors (EDs) representing a number of middle- and low-income countries, including China, India, and Saudi Arabia. These EDs fired back with a letter to the president protesting the US – the Bank's biggest shareholder – attempt to directly influence Bank operations. Moreover, the EDs expressed their objection to developing countries having to take out loans to finance more expensive renewable energy, while climate finance from developed countries has not been forthcoming and the US has not addressed its GHG emissions domestically.

Although the US unilateral approach is unacceptable and the US deserves to be called out whenever possible on the lack of climate finance and lack of action on domestic GHG emissions, it would be a shame to ignore some of the stronger – in climate protection terms – guidance provided in the US coal note. The US guidelines are meant to augment the ambiguous World Bank coal-powered generation guidelines approved by the Board in October 2008. These relatively weak Bank guidelines, it could be argued, have not changed the Bank's approach to supporting mega-coal power projects, especially in middle-income countries (see the Eskom project below).

The US guidelines enhance the World Bank's coal guidelines in four important areas. First, they provide a more detailed, step-by-step approach to the analysis of low-carbon alternatives before making a deal on coal. Second, they differentiate the requirements attached to assistance for coal between middle-income and low-income countries, with more requirements expected from the former. Although, the US guidelines may not necessarily result in less MDB assistance to middle-income countries than the Bank guidelines, there is at least recognition that the approach/requirements should be different.

Third, the US guidelines require more transparency, e.g., public disclosure of the alternatives analysis and of GHG emissions estimates, including the coal project vs. Bank assistance for low-carbon development. Last, the US guidance requires MDBs to make substantial efforts to assist borrowers in seeking external financial resources to cover the incremental costs, should an alternative option to coal turn out to be more expensive. Although the US guidelines are aimed at pushing the MDBs to finance more low-carbon options over coal, the guidelines leave plenty of openings for coal-powered generation to receive MDB funding.

Coal guidelines aside, there are at least two important tests that climate-conscious donors should consider before committing to a capital increase. The first test is to review the Bank's recent and proposed energy-related lending portfolio. The second test is the Bank's forthcoming new Energy Strategy. Currently, the Bank is failing to prove it is a climate-progressive Bank on both of these counts.

The year of coal in 2010?

Even though the Bank has substantially increased financing for new renewable energy and energy efficiency in recent years, the Bank is poised to make FY2010 the year of coal. It has already provided close to USD 2 billion to support coal-powered generation in middle-income countries.

The coal money includes an additional USD 1 billion to India mainly to build a transmission network that can handle the large bulk power transfers stemming from two newly commissioned thermal coal plants, including the Tata Mundra Ultra Mega Power Project, which in 2008 had already received USD 400 million from the IFC. Other coal-powered generation projects include: Central Termoelectrica Andino, Chile, USD 740 million (IFC), and Morupule B Generation and Transmission Project, Botswana USD 379 million (IBRD loan and guarantee).

Most controversially of all, and after a hotly contested prevote consultation, last month the Bank finally approved a USD 3.75 billion loan to Eskom, the South African state owned electricity generator. The bulk of the loan (USD 3 billion) is for construction of the Medupi coal-fired mega power plant (4,764 MW). According to local CSOs, the project will substantially contribute to global warming while failing to provide affordable power for low-income consumers in South Africa. Local communities and environmentalists have protested the Eskom loan, including at the firm's Durban headquarters on February 16.

The Bank loan also includes USD 260 million to support a wind farm and a concentrated solar power (CSP) plant. However, the CO_2 savings that will be attributable to these renewable projects will be modest by comparison to the emissions of Medupi, estimated at nearly 25MMT of CO_2 per annum. The Eskom project has also received support from the African Development Bank – notably, as in the World Bank vote, the US abstained from the vote.

New strategy could draw a line in the dirty energy sand

The second climate-progressive test is the World Bank's new Energy Strategy, which is currently under development and will guide energy-related lending from 2011 to 2021. The Bank conducted the first public consultation in Paris on 17 February, with the face-to-face global consultations continuing until June.

Although the GCI commitments will be decided this month, progress on this front is needed now. The Bank's Energy Strategy Approach Paper, on which the consultations are based, provides a business-as-usual approach to future energy sector development. If the final Energy Strategy follows the Approach Paper, the Bank will continue its lending for mega-coal projects in middle-income countries, making the global transition to low-carbon de-

velopment very difficult. The final Strategy is expected to go to the Board in early 2011.

Without substantial changes to its lending practices and policies, the Bank may want to consider calling itself the "Coal Bank" instead of the "Climate Bank".

Heike Mainhardt-Gibbs, Bank Information Center

Read about Bank Information Center's model World Bank Energy Strategy at: http://www.bicusa.org/en/Article.11859.aspx

Belene in and out of the grip of Russia

Following last October's withdrawal of the German energy giant RWE from the proposed Belene nuclear power project in Bulgaria, it was widely thought that this leftover of communist-era energy policies had finally met its grave. Bulgarian prime minister Boyko Borisov and his energy minister, Traiko Traikov, have been facing, however, a much more complex reality.

On the one hand are the facts that left RWE with no option but to pull out of Belene: the one time 4 billion euro project price tag had spiralled up reputedly to 10 billion, seismic data were tampered with, regional opposition was – and is – as strong as ever, two Bulgarian parliamentary parties openly spoke out against Belene and Borisov's own GERB party is split on the project, hundreds of millions had been squandered on consultants with marginal outcomes, and many tens of millions of initial investment had disappeared. Perhaps above all, the project has become a don't-touch for commercial banks – even the number one atomic bank BNP Paribas was unable to find any funding. Borisov has even called Belene a possible 1 billion euro carp pond during a recent visit.

On the other hand, a large section of the Bulgarian population supports the Belene nuclear plans almost religiously. This support has been whipped up over the last decade by respective governments, but the drip-drip of shocking financial figures and revelations has led to severe cracks emerging in this support, and even the Bulgarian media have started publishing criticism.

Looming large, though, is pressure from Russia: Belene was to be its nuclear entry-project into the European Union, its flagship project for international expansion. Not forgetting too the alleged 800 million euro compensation payment for Russian engineering company Atomstroyexport in case of contract breach.

Thus, in the months following RWE's withdrawal, Russia started a charm offensive: it offered to provide a loan for the first two years of construction investment – 4 billion euros, to be guaranteed by the Bulgarian electricity utility NEK and not, as per an earlier offer from Vladimir Putin, by the Bulgarian government. The latter approach would have been in breach of European state aid legislation and too large a risk for the already shaky Bulgarian budget. Russia also doggedly continues to manufacture large parts for Belene in order to create some sense of project momentum.

Politically, though, Belene is on hold. It is not completed, nor is there any chance it can move forward. The Bulgarian government has announced a fundamental reorganisation of the project, at a certain moment considered a possible decrease in its own participation to as low as 20 percent, then returned to a 51 percent share, and is currently searching for a heroic consultancy that is willing to prepare proposals for a financial structure. HSBC, Societe Generale, a consortium of KPMG and Maguire, Rothschild, Arjil and Ernst and Young are taking the bet. A decision is expected soon.

In the mean time, the Bulgarian nuclear lobby is attempting to divert attention away from the Belene debacle by restarting the discussion about a seventh reactor for the Kozloduy nuclear power plant, 150 kilometres upstream on the Danube.

The arguments that Kozloduy is sited in a less seismic area than Belene, and that already available infrastructure might push down costs, do hold. But the other fundamental flaws that have come to light in the case of Belene will have equal weight when it comes to assessing the chances of an expanded Kozloduy: overall construction costs have priced the nuclear option out of the market, and there is a boom in alternative –especially renewable – generation capacity development in the entire Balkan region that reduces the need for nuclear capacity and is already forcing NEK, as grid operator, to rethink its grid management.

It is unlikely that 1000, 1658 or even more megawatts of inflexible nuclear capacity could find a place on the network in 2020 or beyond. Furthermore, the fundamentally non-transparent environment in which the nuclear industry in Bulgaria operates will prevent banks and other investors from warming to such a white-knuckle ride.

The coming months are looking like being of crucial importance for the future of Bulgaria. Will it be forced back under the influence of Russian centralised planning and large scale engineering paradigms? Or can it break free and be able to develop a modern, secure, robust, decentralised and clean power system based on energy efficiency, renewable energy development and modern grid structures? Given the extent of Russian influence, Borisov does not have an easy choice.

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IFI round-up

Saving of Rospuda Valley in Poland wins environmental 'Nobel' prize

Polish conservationist Gosia Górska was announced in April as one of six winners of the prestigious international Goldman Environmental Prize for leading a successful campaign to stop construction of the controversial Via Baltica expressway through the Rospuda Valley in northeast Poland, one of Europe's pristine wildernesses and an EU Natura 2000 protected site.

Gosia's inspirational campaigning work on behalf of the Polish Society for the Protection of Birds, and involving a wider coalition of activists and organisations, has ultimately resulted in a significant legal precedent for the protection of wilderness habitats across Europe: her challenge to the Polish government has led to the first ever successful intervention by the EU to obtain an order from the European Court stopping a member state from breaching environmental regulations and damaging a Natura 2000 site. This court ruling now has the potential to strengthen the legal framework for EU environmental regulations across Europe, specifically the protection of Natura 2000 sites.

Bankwatch is proud to have been part of this major campaign victory, and we are rolling up our sleeves to work on ensuring the implementation of the new Via Baltica route decision, as well as closely following developments around the Via Carpatia expressway. In spite of the precedent set by Gosia and supporters of the Rospuda campaign, there is no guarantee that the "environmental safety first" message has registered yet with project promoters and developers in Poland and across central and eastern Europe.

For more information, see: www.bankwatch.org/project/Viabaltica

EIB challenged to justify the latest ArcelorMittal public millions

This spring's "rich lists" have seen Lakshmi Mittal, CEO of steel giant ArcelorMittal come in fifth in the Forbes magazine global list, and having doubled his billions in one year Mr Mittal is back at number one in the 2010 Sunday Times Rich List published this month. His company too is experiencing a resurgence: the last quarter of 2009 saw it boasting sales of USD 18.6 billion and profits of USD 1.1 billion.

On 21 October 2009 the European Investment Bank's board of directors approved a loan to ArcelorMittal worth EUR 250 million for a research and development programme said to be all about bringing environmental added value to the company's European operations. The company has a very chequered history over the last ten years in its implementation of environmental improvement schemes that have been financed by over half a billion dollars in public loans, chiefly from the EBRD and the IFC.

Putting the important environmental issues to one side for a moment, couldn't a company the size of ArcelorMittal be expected to either fund such a scheme out of its own resources or be able to access commercial loans, leaving advantageous EIB financing to companies more in need and struggling to plot a course through the economic downturn? And isn't the EIB supposed to only give loans to finance those projects that cannot be entirely financed by the various means available in European member states?

Frustrated by their dealings with the EIB on these matters, Bankwatch, ClientEarth and Global Action on ArcelorMittal have lodged a formal complaint with the Secretary General of the EIB that questions the rigour and ultimate validity of the bank's pre-loan assessment. The complaint remains in process – high time, though, for some public debate about the magnetic pull ArcelorMittal seems to have towards public money.

See the text of the NGOs' complaint in pdf at: http://bankwatch.org/documents/Complaint_EIB_ArcelorMittal_loan_030310.pdf

All a twitter about PPPs

The IFC's Vice President for Business Advisory Services, Rachel Kyte, sent out what can only be interpreted as a mayday message for PPPs over Twitter from Davos in January.

Kyte tweeted: "Need to find new way to say 'public private partnership' Debased by talk and little action. Need for action to scale. So what is it?"

A new name for the highly controversial investment vehicle – and then, in the blink of an eye and the chirp of a tweet, do more of them. No, we don't get it either. Twitter may not be the best medium for laying out responsible investment methodologies.

EIB out of Tenke, paid back prematurely for Chad-Cameroon, still open to Gibe 3 mega dam

The European Investment Bank's appetite for getting tangled up in huge, egregious projects in the developing world must be starting to recede following several announcements in the last few months – that is of course if lessons learned appraisals receive sufficient attention at the bank.

First, the EIB announced that it will not finance the first phase of the Tenke Fungurume mining project in the Democratic Republic of Congo. A range of serious question marks hung over the transparency and pro-development credentials of the project, and despite NGO warnings the EIB had been prepared to approve a EUR 100m loan in 2007, a loan that was made conditional on the Tenke contract passing Congolese government review, which it then failed to do.

Second, announcements are emerging that Chad's government has repaid early an EIB EUR 144m loan for the disgraced development elephant also known as the Chad-Cameroon oil pipeline. The loan had been scheduled for repayment in 2015, but Chad's move has been widely viewed as a way in which to elude hoped for transparent selling of the pipeline's oil. Like the World Bank before it, the EIB's leverage and ability to ensure that development benefits accrue from a major extractives project have been left in tatters.

In the wake of these debacles, Counter Balance: Challenging the European Investment Bank is calling for an independent review of the EIB's engagement with the extractives sector. Meanwhile, Counter Balance and other international NGOs are calling for the halt of the destructive Gibe 3 Dam on Ethiopia's Omo River, a highly ambitious project that sees the Ethiopian government seeking more than USD 1.4 billion from the African Development Bank, the EIB, the World Bank, as well as the Italian and the Kenyan governments.

As Terri Hathaway, director of International Rivers' Africa Program, points out: "Gibe 3 is the most destructive dam under construction in Africa. The project will condemn half a million of the region's most vulnerable people to hunger and conflict." An online petition to stop the man-made disaster of the Gibe 3 Dam has been set up at:

http://stopgibe3.org/pages/doc.php

How long till the penny starts to drop at the EIB about these notorious investments, rather than yet more so-called development billions coursing out of its coffers?

Information on these developments is available at the Counter Balance website: www.counterbalance-eib.org/

Lugar cuts to the chase on reform of the banks

U.S. Senator Richard Lugar illustrated once again his own very due diligence over the workings of the international public development banks with a timely op-ed article in the Washington Times just days before the recent World Bank and IMF spring meetings. Lugar's main concerns – reflecting a recent hard-hitting report from his Senate Foreign Relations Committee – boil down to: investment quality, can we start seeing concrete results; transparency, or lack thereof, and; corruption. If more capital is to come the way of the IFIs, then tangible progress on these key issues needs to be hard-wired into any agreements.

On corruption, Lugar highlights the snail's pace approach that tends to prevail in IFI world: "The development banks, like other large institutions, are often slow to accept and implement these kinds of reforms [vis-a-vis corruption]. For instance, legislation I authored five years ago urged the banks to adopt a policy that any firm found guilty of corruption by one development bank would be blacklisted by all. Only this month did the banks finally take this welcome step."

A slow step forward then as announced by the World Bank, EBRD and other IFIs with the announcement on April 9 of a joint agreement to cross debar firms and individuals found to have engaged in wrongdoing in IFI-financed development projects. But with investments via the opaque 'financial intermediary' (FI) model by the EBRD and the IFC now nudging 40 percent of overall annual lendings, and the EIB still scaling up its own lendings via similar private bank channels, how long will it take for IFI shareholder oversight to establish who and what is really gaining out of these arrangements? The FI model is presenting transparency problems that take us several steps back.

Adding insult to injury: the World Bank and IMF's current legacy in Serbia

In seeking ways in which to recover from its grave economic and social decline of the last two decades, Serbia has had little choice but to rely on advice and financial support from international bodies like the International Monetary Fund (IMF) and other international financial institutions (IFIs). The beleaguered state thus opted to direct itself toward a free market – or 'neoliberal' – economic footing, where the rule of law would be established and foreign direct investment and resources attracted for the economic and social revival of Serbian society.

After the finalisation of an arrangement with the IMF in 2005 under the rule of a conservative and moderate rightist government, Serbia attempted the reform and improvement of its economy, but this time without IMF advice.

Unfortunately this effort was undertaken without effectively tackling and addressing endemic structural challenges in the national economy and with far too little emphasis on reversing Serbia's resource intensive, low profit, energy consuming sectors of production and consumption. In 2005, the International Energy Agency noted that Serbian industry's use of energy was three times more wasteful than the EU average when it came to producing a unit of GDP; the recycling sector accounted for just 0.3 percent of Serbian industry, vividly illustrated by the fields of junk visible when travelling in most parts of the country.

By 2008, then, industrial output was at only 52 percent of the industrial output of 1990, with 250,000 fewer people officially employed. Yet Serbia was showing all the signs of an economy oriented towards achieving low inflation, stable exchange rates, cutting the number of employed people in the public sector (without establishing new sustainable sectors of the economy and new production) and relying on enormous IFI-backed loans in so doing. At the same time it was supporting, at any cost and without much in the way of rigorous assessment, any company that expressed an interest – and at least minimal capability – in exporting anything. Serbia's imports were also spiraling, with acute problems cropping up in the importing of energy and resources needed for mining and heavy industry.

Serbia's crisis pre-dates the big crisis

In early 2008, Serbia was once again forced to call upon the IMF to help counter financial and budgetary problems. It may have been overlooked as the global financial and economic collapse in the second half of 2008 swept everything before it, but at least six months prior to the snapping of the global tightrope Serbia was already showing strong signs of structural weaknesses accompanied by the contraction of economic activity.

This downward economic spiral, according to widely-held opinion, was ignited after the large-scale privatisation of the country's most profitable and lucrative assets – large cooperatives with major landholdings, including beer and milk producers, the tobacco industry and cement manufacturing, Smederevo steel melting, the mobile telephony sector and metal manufacturing factories across the length and breadth of the country.

This ran concurrently with substantial structural and fiscal changes, implemented as per IMF and World Bank prescriptions, including zero percent tax rates on capital profits and on financial market gains. Indeed, Serbia's current prime minister, Mirko Cvetković, himself an economist by training, has pointed out that as a result of these structural changes the percentage taken by the services sector – financial services, telecoms and retail sectors – in Serbia's GDP has become excessive.

In its first approach in 2008 to the IMF, Serbia requested USD 500 million for macro-economic stability and to protect the exchange rate. Just a few months later, however, it became apparent that the national budget deficit would result in breakdown and thus Serbia requested a new program with the IMF involving in excess of USD 2 billion.

Yet the country's economic output patterns reveal that programs focused exclusively on fiscal and budgetary issues to the detriment of really tackling the structure of production for the medium and long term development of the economy have resulted in dead-end results.

Once again, throughout negotiations in 2009 and 2010, the IMF showed its inability to register and respond to the deep-lying causes of almost permanent crisis in Serbia. The Fund overlooked the much needed structural changes that could have helped to deliver greater social and economic justice, diversification of the economy towards sustainable energy and a more resource-efficient economy that places enhanced emphasis on decent work, solidarity, knowledge and innovation.

Fund familiarity breeds more contempt

The IMF prescriptions for Serbia that featured in three weeks of negotiations with the country's top decision-makers in February 2010 were in fact highly familiar extracts from the Fund's conventional playbook that have proved to be so deeply unpopular in many countries around the world in previous decades: privatisation, the reduction of pensions and the number of pensioners, the raising of the age for pension provision, a low single digit inflation rate, the stabilisation of the exchange rate, and the freezing of salaries in the public sector with significant cuts in the number of public sector employees.

The upshot was a period of uncertainty and stress for millions of people living on the edge of or below the poverty line, for the 1.6 million pensioners and 800,000 people working in the public sector with precious few assurances that these measures will stave off the further economic and social demise of Serbia.

Yet the backlash is mostly felt by these members of the public, viewed as reform-shy laggards by the legions of economists and government advisors happy to toe the line insisted on by IMF and World Bank programs. While criticism of popular resistance to these measures comes readily, level-headed analysis of the consequences of IMF policies and World Bank programs from its proponents tends to be all too rare.

Pensioners feel the squeeze

"The essence of reform in Serbia," offered Dijana Dragutinovic, Finance minister for the Republic of Serbia, in February this year, "is the reduction of the number of pensioners." The minister did little more than echo the prescriptions of IMF representatives during the stand-by arrangement negotiations, this despite the presence of the Pensioner party in the coalition government. Standing at 12 percent of Serbia's GDP, the established rights of pensioners would appear to count for very little in the current dominant logic – and have been a major stumbling block in the process of the IMF negotiations.

The Pensioner party had won significant electoral support that eventually saw it entering the ruling coalition in early 2008, primarily because of the World Bank's Structural Adjustment Program (SAP) that sought devastating reform of Serbia's pension system. If the pension reform plans included in the SAP from 2001 and SAPII from 2005 had been implemented, then the average pension in Serbia would not be the 63 percent of the average salary it is today but 39 percent. Serbia officially has 1.6 million pensioners. A quarter of a million of these pensioners receive less than EUR 1200 per year. The proposed reforms were not fully implemented because of strong opposition from the pensioner and opposition parties that resulted in the parties ultimately joining forces in the coalition government.

The IMF and the World Bank had been proposing throughout the negotiating process in 2001-2005 and in 2009 to link pensions to the cost of living, despite the fact that under this calculus pensions have fallen under 60 percent of net average income; at the same time the IMF proposed that the pension age for women and men become the same: 65.

The Pensioner party and the Association of pensioners argued successfully for pensions to be calculated not only in connection to the cost of living but also to the growth of real salaries, which as they pointed out is regulated in an annex of agreement with the IMF. However, disaster for more than 1.6 million pensioners in Serbia will be incurred if the adjustment of the minimum pension is not linked to salaries in the public sector throughout 2010 and 2011. The pensions minister is currently seeking to assure this large section of the population that he will be able to protect pensioners from hefty cuts to their incomes.

Public versus private ... or private over public at all costs

According to World Bank documentation on Serbia for financial year 2009: “Substantial progress was made in strengthening the legal framework in the area of corporate governance and competition. Further, the government has continued with the reforms aimed at strengthening financial discipline and achieved substantial progress in the area of restructuring, privatization, and bankruptcy of socially owned enterprises and enforcement of hard budget constraints, continued reforms in the energy sector, and establishment and development of a state audit institution. The government has made substantial progress in implementing its program of restructuring and privatization of designated state owned banks, insurance companies, and financial assets. Additional measures were implemented for strengthening insurance sector regulation and resolution regime, enhancement of prudential supervision of the banking sector, as well as strengthening capital markets regulatory and supervisory regime”.

However much of the evidence related to the sectors cited above points in different directions.

Besides state pensions, another problematic area in the negotiations with the IMF and the World Bank was the size of Serbia's public sector. Already weak and understaffed in a number of sectors – for example, health care, education and various inspectorates – the public sector is in line to be further squeezed in terms of resources and employees. This is a very familiar neo-liberal measure and it places major question marks over the regulation of the economy and social protection – in Serbia, though, the need for a healthy public sector is as necessary as ever.

The privatisation of companies under the auspices of the World Bank's SAP I and II was planned for finalisation – at any cost – by the end of 2010. The target was to privatise all publicly owned companies by this time including as many as possible of the public utilities present in local communities, such as electricity companies, telephone companies and industrial interests, such as mining. It was a hastily and badly prepared process and unfortunately it has lead to deeply negative results on different levels.

Out of 2291 privatised companies, already 513 contracts have been terminated due to non-compliance with obligations proceeding from contracts. An additional 700 companies are on the brink of contract termination. In January 2010, out of 134 controlled companies, 30 contracts were terminated.

“Privatisation in Serbia was one of the most corrupt processes in the entire world,” Verica Barac head of the National agency for the fight against corruption and fraud commented in the weekly paper Ekonom in February this year. “It was the only privatisation wave in central and eastern Europe where more than 30 percet of the reports that preceded privatisation, and which where prepared by the national Agency for Privatisation, were in fact false and fraudulent! It's also very hard to estimate the percentage of capital invested that is in fact tax evasion or money laundering, but in the case of money laundering there are estimations of at least 5 percent of GDP, or up to EUR 1.5 billion!”

It is clear that privatisation was a channel for money laundering and tax evasion on an unprecedented scale. Recent arrests have revealed, for instance, the existence of an enormous Europe-wide cocaine cartel based in Serbia and North Montenegro (Šarić group) that demonstrates the depth and the extent of corruption and reveals the weaknesses of the state and its agencies in Serbia. The Šarić group supported at least 50-100 privatisations, and succeeded in purchasing at least 15000 hectares of the best fields in the Vojvodina province.

Indeed, some of the best Serbian foreign-private investors are based in Cyprus, Luxembourg, London and other less well-known exotic tax havens. These companies own huge assets and are key players in some sectors, even having monopolies in others. These facts rarely reach the Serbian media because much of the media is heavily sponsored or owned by companies or daughter companies of tax-evading businesses. The acuteness and scale of the financial damage being caused by these direct or indirect evasions has never been publicly estimated in Serbia.

Dirty money is also widely believed to have aided the privatisation of public transport companies, and more generally Serbia's economic landscape is filling up rapidly with ruins and wrecks:

- There are bleak estimations that more than 60,000 private companies are illiquid and that their accounts have been blocked.
- There are estimations that at least 100,000 people working in the private sector, out of an estimated total of 900,000, are working without being paid regularly or at all.
- Significant parts of the agricultural sector, building industry and the financial sector are heavily financed by resources accrued from tax evasion and money laundering.

On top of this, fiscal reforms introduced in 2001 under the World Bank's SAP I have led to the raising of taxes and the development of Serbia's current tax system where average salaries are taxed (alongside social and health contributions) at an increasingly higher rate and the overall tax burden for the upper and highest ranges have been progressively lowered: 41 percent for average salaries to 34 percent for incomes that are more than eight times the national average salary.

Given the evolution of such a terminally regressive taxation system, it is only natural that there is next to no incentive for legal employment and new working places. The relevant ministries do not want to reveal how much private and public companies owe to pension funds and health care. Not surprisingly the state is not able to collect all the planned budgetary resources when even public companies are employing people either illegally or at the lowest permitted salary, with the rest paid in the hand without tax. It goes without saying that the enforcement of tax collection and the enforcement of laws protecting the rights of workers and the environment are the weakest links in the Serbian economy's rusty chain.

Crisis loans in Serbia

All of these grim facts illustrate how deep and misguided are the attempts to achieve a fully liberalised Serbia, via for instance non-regulated privatisation. Is this the way to promote and achieve sustainable economic development? The crisis loans that have been accumulating from the IMF and the IFIs since 2009 would suggest no, but the very implementation of these loans doesn't appear to be helping matters much either.

In the first quarter of 2009, the Serbian goverment, with the support of the IFIs and the IMF, started to specifically support the liquidity of Serbian companies, in particular export oriented companies, as well as programs of support aimed at saving jobs in some of these companies. This resulted in the disbursement of 11,673 such loans totalling EUR 936 million, of which almost half was used by companies employing more than 100 people. Yet the same companies that asked for liquidity support are, one year on, asking for the same support, suggesting that they are structurally not in good shape for business. This also shows that the disbursement of these crisis funds is happening without really asessing the potential and sustainability of the companies involved. Moreover, the sustainability of these companies in terms of environmental and social aspects is never given a mention.

So, stimulus programmes, backed by foreign loans that are only adding to Serbia's indebtedness, are not proving to be effective. Jobs have been axed in the private sector, and daily strikes and protests tell the story of failed privatisations. The National Bank of Serbia points out that external liquidity and solvency indicators are showing Serbia to be a middle-indebted country. Foreign debt on September 30, 2009 was almost identical to the figure from the year before, but in terms of GDP it rose by 5.8 percent, reaching 70.4 percent of GDP. Private sector debt reached EUR 14.9 billion in October-November 2009; public debt totalled EUR 9.9 billion.

So, how should the government act, and in which direction should it turn? Unfortunately, a concentration of so-called 'stimulus' investments in highly unsustainable sectors seems to be the preferred – and sole – focus: coal-fired power plants, gas storage facilities, petro-chemicals, and the dirtiest possible mining and smelting industries are all being proposed and developed alongside highway building.

All of these programs and projects fall within the orbit of the IFIs and will lead to the further indebting of Serbia, not to mention its longer term inability to service its debts. These sectoral developments will not ensure new employment in the longer term, because most of these projects will be developed and implemented as “key in the hand” from the side of foreign businesses. Under such circumstances foreign companies practically import their own workers, produce parts in their countries of origin, and introduce their technical knowledge without any transferring of skills and technologies to the country of supposed investment – in this case Serbia.

U turn needed to escape a dead end

With Serbia's economy not so much in the doldrums but in a long-term downward spiral, the experimentation with and indulgence of the blind hand of the free market must now be reined in.

To replace it, the basic concepts of welfare and solidarity should come to the fore, with the establishment of

sustainable jobs being the top priority. The government, unions and banks operating in Serbia should be allowing these basic ideas the space to breathe as an integral part of their policies and programmes.

If, as now seems unavoidable, investments in heavy infrastructure, dirty energy and industry are seen as the short-term option for Serbia, then the principle of the 'Polluter Pays' has to be at the the heart of any programming that underpins their introduction.

Besides this principle, the principles of democratic participation, fiscal decentralisation and the decentralisation of decision-making can help to ensure that the interests and well-being of local communities and underdeveloped regions are taken in to account within the complicated algebra of sustainable development.

If there is one starkly evident lesson to be learned from social and economic experiences in Serbia since the turn of the century, it is that the IFIs and the IMF should not be entrusted with the role of leading development institutions in their countries of operation. Instead, in Serbia and in other countries struggling to get a toe on the development ladder, these institutions should be supportive mechanisms, ones that neither impose the direction of development over sovereign countries nor insist that global 'solutions' ride roughshod over national and local ones.

Bank watchdog boycotts ADB annual meeting in Tashkent

The NGO Forum on the ADB is boycotting the upcoming 43rd annual meeting of the Asian Development Bank in Uzbekistan. The bank watchdog slammed the ADB's decision to hold the meeting in Uzbekistan, pointing out the track record of the government when it comes to human rights violations and the curtailment of people's freedom of expression.

Announcing the boycott, Forum Executive Director Dr Avilash Roul commented: "The ADB's decision to hold its annual meeting in Tashkent is not only non-transparent but also endorsing suppression of human rights and people's freedom of expression,"

In the central Asian state, political rights are severely constrained and dissent is not tolerated, often being met with extreme force, the NGO Forum on the ADB said in a statement. Parviz Umarov of the Tajikistan-based Center for Development of Civil Society said: "As there are no vibrant civil society groups in Uzbekistan, it is impossible to hold public opinion in the venue of the annual meeting or outside by looking at the political situation in the country,"

In a letter submitted to the bank last January, the Forum requested the ADB to guarantee the safety, security and well-being of civil society participants in the 43rd annual meeting, as well as their right to assemble and discuss development-related issues, distribute printed materials related to the ADB's operations, and peaceful protest. However, until now, the multilateral bank has kept its silence on the matter.

"As a multilateral public entity, the ADB must respect the rights of local communities to development and livelihood rather than just serving the interests of undemocratic, arrogant governments and businesses," commented Hemantha Withanage of the Sri Lankan Centre for Environmental Justice.

In March this year, the UN Human Rights Committee scrutinised Uzbekistan's rights record and expressed its concerns over "the number of NGOs, journalists and human rights defenders imprisoned, assaulted, harassed or intimidated because of the exercise of their profession."

"The ADB's move only shows that it is more inclined to holding its meetings in such an autocratic regime where the freedom of speech is severely restricted," Dr Avilash Roul continued.

Last year's ADB annual meeting in Bali, Indonesia saw local activists being harassed by security. "Police and intelligence were stationed in our hotel, our vehicles were stopped several times on our way to the annual meeting venue which gave us no choice but to cancel our meetings with some of the ADB's board of directors," recalled Wardarina of Solidaritas Perempuan, Jakarta..

The NGO Forum on the ADB is a 250-strong Asian led network of civil society organisations which has been monitoring the ADB's policies, projects and programs since 1992.

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