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**REPORT FROM THE COMMISSION  
TO THE EUROPEAN PARLIAMENT AND THE COUNCIL  
ON BORROWING AND LENDING ACTIVITIES  
OF THE EUROPEAN COMMUNITIES IN 2007**

**{SEC(2008)2504}**

(presented by the Commission)

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## 1. INTRODUCTION

The Council decisions establishing the various lending instruments of the European Communities require the Commission to inform the Council and European Parliament, each year, of the use of these instruments. In order to meet these information requirements, this report describes the lending operations for each of the areas concerned.

In particular, the respective Council decisions<sup>1</sup> for lending activities outside the Community require the Commission to inform the Council and Parliament on an annual basis of the situation regarding European Investment Bank (EIB) financing operations (loans and loan guarantees) guaranteed by the Union budget in the Pre-Accession Countries, the Mediterranean, Eastern Europe, Southern Caucasus and Russia, Asia and Latin America and the Republic of South Africa.

To complete the picture of lending activities, the report gives a brief summary of the borrowing activities undertaken in order to finance the lending activities, of the macro-financial assistance provided by the Community to third countries and of the interest subsidies and guarantees associated with Community loans. In addition, it provides information on Euratom lending activities.

More detailed information on the above activities, including statistical tables, is provided in the attached Staff Working Paper (hereinafter referred to as the "Annex")<sup>2</sup>. References to Tables in this report are to the Annex unless otherwise stated.

## 2. BORROWING ACTIVITIES

In order to finance the lending activities decided by the Council, the Commission is empowered to borrow, on behalf of the respective Community (EC, Euratom) funds on the capital market<sup>3</sup>.

Total borrowing by the European Communities and the EIB increased in 2007 by 13.8% to EUR 54.7 billion, against EUR 48.1 billion the previous year (see table and graph in Section 1.1 of the Annex). This substantial increase is mostly due to a higher rhythm of disbursements of EIB loans which induced an increase in the borrowing programme during the year. The EIB also found market conditions very supportive as, in the wake of the sub-prime crisis, demand for first class instruments like those offered by the Bank strongly increased.

Regarding the European Communities, borrowing activities are based on decisions concerning Euratom, macro-financial assistance and balance-of-payments loans. An amount of

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<sup>1</sup> Council Decision 97/256/EC, as amended by Council Decisions 98/348/EC and 98/729/EC, covering the period 01.02.1997-31.01.2000 (the "1997-2000 General Mandate"), and Council Decision 2000/24/EC, as amended by Council Decisions 2000/688/EC, 2000/788/EC, 2001/778/EC, 2005/47/EC and 2006/174/EC, covering the period 01.02.2000-31.01.2007 (the "2000-2006 General Mandate"). Council Decision 1999/786/EC (Turkey Earthquake Reconstruction and Rehabilitation Action (TERRA)) forms an extension of the general mandates. Furthermore, Council Decision 2001/777/EC established a special lending action for selected environmental projects in the Baltic Sea basin of Russia under the Northern Dimension. Council Decision 2005/48/EC established a separate mandate for certain types of projects in Russia and Western NIS (Ukraine, Republic of Moldova and Belarus). Finally, Council decision 2006/1016/EC established a new general mandate covering the period 01.02.2007-31.12.2013 (the "2007-2013 General Mandate").

<sup>2</sup> SEC(2007)[...]

<sup>3</sup> As the ECSC Treaty expired in 2002, there has been no new borrowing.

EUR 39 million was raised for Euratom in 2007 based on a decision approved in 1994. A new decision for macro financial assistance of EUR 50 million was adopted on 10 December 2007 but did not involve any disbursements and corresponding borrowing in 2007. The intention is to disburse the loan in two equal tranches starting in 2008.

Taking into account repayments, cancellations and exchange-rate fluctuations, the total amount of borrowings outstanding at 31 December 2007 was EUR 255.4 billion, up 2.8% from 2006 (see Table 1.2).

The share of EUR-denominated and Non-Community currencies in borrowings are provided in section 1.3 of the Annex (see Table 1.3).

### **3. LENDING IN NON-MEMBER STATES**

#### **3.1. Overview**

Financial support for non-member States that have concluded cooperation agreements with the Community takes a variety of forms depending on the geographical areas concerned and the objectives pursued.

Financial operations administered by the Commission under decisions of the Council generally take the form of bilateral loans (macro-financial support or balance-of-payments support), where the Community helps to re-establish a country's macro-economic balance.

Loans granted by the EIB from its own resources are either in the form of direct financing for individual projects or global loans to banks, which then allocate funds to smaller-scale local projects. Some of these loans benefit from a guarantee of the Union budget and are, unless otherwise specified, the focus of this report. Under the 2007-2013 General Mandate, the EIB can also provide loan guarantees. A wider spectrum of financial instruments (ranging from equity to senior loans) is used by the EIB when it manages Community or Member States' resources (notably in the Mediterranean and ACP countries).

The Euratom lending instrument<sup>4</sup> is available for financing operations in EU Member States and certain non-member States (Armenia, Russia and Ukraine).

The geographical regions in which the Community conducts lending activities in 2007 are listed in Tables 2.1 and 2.2.

#### **3.2. The Community's Macro-Financial Assistance**

Macro-financial assistance (MFA) in the form of loans is, by its very nature, exceptional and forms part of the efforts of the international community to provide, in conjunction with the Bretton Woods institutions, balance-of-payments support to certain countries facing transitional macro-economic difficulties. MFA focuses on neighbouring regions, such as the Western Balkans and the Caucasus. Disbursements are subject to the beneficiary countries meeting objectives for macro-economic stabilisation and structural reforms. In these circumstances, the number of operations undertaken each year is limited, and it is difficult to make valid comparisons for the assistance given from one year to the next.

Grants and loans disbursed under this instrument are listed in the Table 2.2. A new MFA decision was taken in 2007 providing financial assistance to Lebanon in the form of

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<sup>4</sup> Council Decision 77/270/Euratom, as amended by Council Decision 94/179/Euratom. The ceiling for borrowing to fund Euratom lending was originally fixed by Council Decision 77/271/Euratom. Subsequently, the ceiling was raised by various amendments of the latter decision, the latest of which (Council Decision 90/212/Euratom) increased it by 1 billion ECU to 4 billion ECU.

EUR 50 million in loans and up to EUR 30 million in grants. Disbursements should start in 2008. More information is given in the annual Commission Report on the implementation of MFA to third countries<sup>5</sup>.

### **3.3. EIB Financing Operations under the Lending Mandates**

This section, completed by the information in the Annex, constitutes the annual report for 2007 to be submitted to the European Parliament and the Council in accordance with Article 2 of Council Decision 2000/24/EC and Article 6 of Council Decision 2006/1016/EC.

During the year 2007, two – partly overlapping – EIB external lending mandates have been in force, as the 2000-2006 General Mandate expired on 31 January 2007, but was extended to 31 July 2007 for those geographical areas where the lending ceiling had not been reached, while the 2007-2013 General Mandate entered into force on 1 February 2007. The first loans under the new framework were signed in the second half of the year, following the signature of the new EIB/Community Guarantee Agreement in August 2007.

Until 31 July 2007, lending continued under the 2000-2007 General Mandate in all regions except the Mediterranean, where the mandate sub-ceiling had been reached at the end of 2006. A summary of EIB lending activity in the relevant regions since 2000 is presented in section 2.3 of the Annex.

Under both mandates, the Commission is required to inform the European Parliament and the Council on an annual basis of the operations carried out under mandate, their contribution to the fulfilment of the external policy objectives of the EU, taking into account the operational objectives of the EIB, and to submit an assessment of the coordination and extent of cooperation between the EIB and other International Financing Institutions (IFIs) operating in the areas covered by the mandates. Furthermore, under the 2000-2006 General Mandate, the Commission is required to report on progress made on risk-sharing under Article 1(3) of Council Decision 2000/24/EC. Finally, under the 2007-2013 General Mandate, the Commission is required to assess the extent of cooperation between the EIB and the Commission.

Due to the limited number of operations under the 2007-2013 General Mandate in 2007, the assessment of the impact and effectiveness of EIB Financing Operations as well as their contribution to the fulfilment of the external policy objectives of the EU, including the cooperation with other IFIs and with the Commission, is included in this report and the Annex. However, in the future this assessment will be the subject of a separate report, starting next year, when the number of operations is expected to grow substantially.

Finally, section 2.19 of the Annex includes sectoral and regional tables of EIB financing in Africa, Caribbean, Pacific and Overseas Countries and Territories (ACP/OCT) in 2007. These operations, carried out in the framework of Cotonou Partnership Agreement and the Overseas Association Decision, do not fall under the Community Guarantee and are therefore not covered by this report. The EIB 2007 Annual Report on the Investment Facility under the ACP-EU Cotonou Partnership Agreement is available at [www.eib.org](http://www.eib.org).

#### **3.3.1. Volume of Operations**

In 2007, the Bank signed loans amounting to EUR 3,723 million, of which EUR 1,825 million under the 2000-2006 General Mandate (expired on 31 July 2007) and EUR 1,898 million under the 2007-2013 General Mandate.

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<sup>5</sup> Not yet published for 2007. For 2006, see COM/2007/0493 final.

Table I below provides an overview of EIB external lending under the Community-supported mandates in 2007, split by sectors and geographical region. The individual loans are listed in section 2.13 of the Annex, while the aggregate distribution of lending volumes by mandate is presented in its section 2.4.

*Table I: Sectoral breakdown of mandate loans signed in 2007 (EUR million)*

Region	Grand Total		Transport infrastructure		Credit lines		Energy		Industry & Services		Telecommunications		Water, sewerage	
Pre-Accession Countries	1,750	100%	827	47%	420	24%	103	6%	400	23%	0	0%	0	0%
Mediterranean	1,205	100%	180	15%	625	52%	280	23%	0	0%	0	0%	120	10%
Eastern Neighbours	230	100%	230	100%	0	0%	0	0%	0	0%	0	0%	0	0%
Asia and Latin America	425	100%	28	7%	0	0%	0	0%	0	0%	310	73%	87	20%
South Africa	113	100%	0	0%	0	0%	88	78%	25	22%	0	0%	0	0%
<b>Total</b>	<b>3,723</b>	<b>100%</b>	<b>1,265</b>	<b>34%</b>	<b>1,045</b>	<b>28%</b>	<b>471</b>	<b>13%</b>	<b>425</b>	<b>11%</b>	<b>310</b>	<b>8%</b>	<b>207</b>	<b>6%</b>

### 3.3.2. Progress Made on Risk-Sharing

The 2000-2006 General Mandate invited the Bank to "aim to cover the commercial risk on 30% of its lending under this Decision from non-sovereign guarantees as far as possible on an individual mandate basis. This percentage shall be expanded upon whenever possible in so far as the market permits".

As can be seen in Table 2.4, at the overall mandate level risk-sharing loans represented 19% of total cumulative signatures at expiry of the 2000-2006 General Mandate. However, this figure covers significant regional differences:

In Asia and Latin America (ALA), where the mandate specifically focused on supporting private European initiatives in foreign direct investment, transfer of technology and know-how, 74% of loan signatures were made under the risk-sharing scheme. In the Mediterranean, South-Eastern Neighbours and South Africa, projects financed under the mandate were mainly in the public sector without risk-sharing arrangements. The proportion of risk-sharing loans reached 11% of total cumulative signatures in the Mediterranean and in South Africa, while the respective proportion in South-Eastern Neighbours was 12%.

Beyond risk-sharing operations carried out under Community mandate, the EIB pursued operations at its own risk under different facilities with total signatures in 2007 reaching EUR 1.86 billion, thereby reflecting the EIB's increased propensity to take commercial risk:

- Signatures under the replenished Pre-Accession Facility amounted in 2007 to EUR 1.18 billion, of which Turkey received 70% and Croatia 28%. The geographical coverage of lending under the Pre-Accession Facility was extended to include the potential candidate countries.
- Under the Mediterranean Partnership Facility II, an EIB loan amounting to EUR 185 million was signed to finance the capacity expansion of one of the priority energy TENs.

- Finally, under the Facility for Energy Sustainability and Security, a highly visible EUR 500 million multi-investment scheme was signed in China to support investment projects in the energy and industrial sectors that will help to prevent or reduce greenhouse gases and other polluting emissions.

### 3.3.3. Contribution to External Policy Objectives

The general lending priority for the EIB in regions outside the EU is to support the Community's policy objectives. Specific regional objectives (depicted in Table II below) are set out in detail in the preamble to Council Decision 2006/1006/EC, with the protection of the environment and energy security as common objectives throughout the different regions.

Table II: Summary of key lending objectives.

Lending Objectives	Asia & Latin America	Eastern Neighbours & Russia	Mediterranean	Pre-Accession Countries	South Africa
Energy - Security of Supply	X	X	X	X	X
Environmental Protection and Improvement	X	X	X	X	X
Private Sector Development, SMEs			X	X	X
Infrastructure Development, including extension of TENs		X	X	X	X
Pre-Accession support				X	
Support of EU presence (FDI, transfer of technology and know-how)	X				

The **energy sector** absorbed 13% of lending under mandate in 2007. The EIB financed energy investment in Egypt (two gas-fired combined-cycle power generation units), Morocco (hydro-powered electricity projects), Bosnia-Herzegovina (rehabilitation of hydropower plants and distribution facilities) and South Africa (construction of high voltage power transmission interconnection).

In total, EUR 938 million or 25% of EIB financing under mandate contributed to the Bank's overarching goal of promoting **environmentally sustainable development** in partner countries. In Pre-Accession countries, projects financed in 2007 under mandate with specific environmental protection as the main lending objective accounted for EUR 731 million or 42% of total lending in the region. These consisted of public transport projects in Turkey and a renewable energy project in Bosnia-Herzegovina. In the Mediterranean, as regards the water sector, EUR 120 million was advanced for environmental schemes in Israel, namely for the improvement of environment and health through provision of safe drinking water. This same objective was also targeted by a EUR 60 million project in Asia for the extension and upgrading of water supply and distribution infrastructure in Greater Manila, and by another EUR 27 million project in Latin America for the improvement of sanitation and environmental conditions in Panama City.

Credit lines in support of **private sector development** represented 28% of total lending, of which the main share was granted in the Mediterranean: Jordan, Lebanon, Syria and Tunisia.



Credit lines supporting SMEs represented more than half of total lending volume in the Mediterranean in 2007. Pre-Accession countries were the second recipient group, with 40% of total credit line volume benefiting Bosnia-Herzegovina, Serbia and Turkey. Industry and services were both represented by one project respectively in South Africa, for the expansion of a particle board and medium density fibreboard factory, and in Turkey, for the strengthening of the country's science and research capabilities. This combined sector represented 11% of total lending.

**Transport infrastructure**, including rail, road, port and urban transport infrastructure, accounted for one third of total lending under mandate in 2007. The majority (65%) of the loans in the transport sector were granted in the Pre-Accession countries, namely Turkey, Serbia, Bosnia-Herzegovina and Albania. The construction or upgrading of railway infrastructure took 76% of this financing in the Pre-Accession countries while the development of transport axes linking to TENs represented 24%. The rehabilitation of road infrastructure axes connecting to priority TENs were also the targets of the first loans granted in the Eastern Neighbourhood countries of Ukraine and The Republic of Moldova. Together with these two operations, the extension of transport TENs accounted for 34% of total transport lending. Two further transport projects were financed under mandate in Morocco (construction of a section of toll motorway) and Uruguay (expansion of private container terminal at port of Montevideo). 8% of total lending was absorbed by the **telecommunications** sector for the financing of two projects in Latin America. In Peru, a project covers the purchase and installation of systems for provision of telephony, high-speed internet, data transmission, cable and satellite pay-TV and VSAT services. In Brazil, a project concerns the installation, commissioning and operation of GSM overlay network in order to migrate from CDMA to a GSM network.

The ALA region is the foremost recipient of EU **foreign direct investment** (FDI) in the emerging countries. Accordingly, within the parameters of the ALA mandates, the bulk of the EIB financing activities in ALA so far have supported EU presence through FDI.

The EIB assesses the value added of its operations on the basis of a framework structured along the following three pillars<sup>6</sup>:

Pillar 1 - the consistency with and contribution to EU policy objectives;

Pillar 2 - the quality and soundness of the project; and

Pillar 3 - the financial and non-financial contribution made by the EIB to the project.

Each individual financing operation is assessed against this framework, using a set of relevant indicators. 84% of EIB operations signed under mandate in 2007 were judged by the EIB to be highly consistent with and to make a strong contribution to the mandate objectives and priorities. This is reflected in the assignment of a "high" rating on Pillar 1. The proportion of "high" ratings in Pillar 2 represented 39% of projects; "medium" was attributed to 55% of projects. Under Pillar 3, 81% of projects were assessed to benefit from "high" EIB contribution, while 16% were rated "medium".

#### *3.3.4. Co-operation with the Commission*

Council Decision 2006/1016/EC invites the Commission and the EIB to strengthen the consistency of EIB actions with EU policies, mainly through a regular and systematic dialogue and early consultation on policies, strategies and project pipelines. To this end, the

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<sup>6</sup> See also section 2.6-2.8 of the Annex.

EIB and the Commission signed a specific Memorandum of Understanding (MoU) defining the terms and conditions of this strengthened cooperation on 26 May 2008.

With a view to enhancing the coherence of overall EU support in the regions covered by the external lending mandate, opportunities are sought to combine EIB financing with EU budgetary resources as appropriate, through, *inter alia*, the Instrument for Pre-Accession Assistance (IPA), the European Neighbourhood and Partnership Instrument and, for South Africa, the Development and Cooperation Instrument.

For the benefit of the Mediterranean region, in order to underpin the financial support provided from EIB own funds, the EIB manages EU budgetary resources in three domains: technical assistance, risk capital and interest subsidies attributed to selected EIB loans, as detailed in section 2.11 of the Annex.

In addition, the Commission and the EIB cooperated in establishing the EU's Neighbourhood Investment Facility, which will mobilise additional funding for infrastructure projects mainly in the energy, transport and environment sectors in the entire area of the European Neighbourhood Policy by providing grant support for lending operations of the EIB and other EU public financial institutions. Close coordination between the Commission and the EIB is also taking place in the context of EU financial instruments in support of the Western Balkans under the IPA.

#### *3.3.5. Co-operation with other IFIs*

During 2007, the EIB actively pursued its policy to enhance the effectiveness of its operations by further reinforcing and developing its operational partnerships with other IFIs.

The Tripartite Agreement between the Commission, the European Bank for Reconstruction and Development (EBRD) and the EIB, signed at the end of 2006, for operational cooperation activities in Eastern Europe, Southern Caucasus, Russia and Central Asia, has started to be implemented in 2007, with a close dialogue between the three institutions and the establishment of a joint pipeline. The EIB and the EBRD are also closely associated in other initiatives and partnerships (e.g. Joint Assistance to Support Projects in European Regions (JASPERS) technical assistance initiative in the framework of EU regional policy).

Furthermore, during 2007 the EIB entered into formal collaborations with other IFIs in the environmental field: the Multilateral Carbon Credit Fund with the EBRD, the Carbon Fund for Europe set up with the World Bank and the EIB-KfW Carbon Program. Finally during the 2007 EIB Forum in Ljubljana, the Post-2012 Carbon Credit Fund was launched, being the direct result of on-going cooperation in the field of climate change between the EIB and three leading European national financing institutions, namely Instituto de Crédito Oficial, KfW and the Nordic Investment Bank (NIB).

The EIB, EBRD, CEB, NIB and the Nordic Environment Finance Corporation remained committed to the terms of the European Principles for the Environment, strongly supported by the Commission.

Other details are provided in section 2.9 of the Annex.

## **4. BUDGETARY IMPACT OF LENDING**

Lending activities have an impact on the Union budget when they are accompanied by Community guarantees, interest subsidies or special conditions comparable to risk-bearing operations for the lender.

#### **4.1. Budget Guarantees**

On 22 December 2004, the Council decided to amend Decision 2000/24/EC to take into account the enlargement of the EU and the European Neighbourhood Policy (Council Decision 2005/47/EC<sup>7</sup>).

The Community guarantee is restricted to 65% of the aggregate amount of the credits opened, plus all related sums (compared with 70% under the 1997-2000 General Mandate). Furthermore, on 22 December 2004, the Council granted a Community guarantee to the EIB against losses under loans for certain types of projects in Russia, Ukraine, Republic of Moldova and Belarus (Decision 2005/48/EC<sup>8</sup>). The overall ceiling of the credits opened is EUR 500 million and the EIB benefits from an exceptional Community guarantee coverage of 100%.

The guaranteed lending period expired on 31 January 2007 and was automatically extended by six months as the lending ceilings had not been reached by this date.

During 2007 (the last year of the 2000-2006 General Mandate) the EIB signed loan agreements of EUR 1 595 million, bringing total lending under this mandate (EUR 20 060 million<sup>9</sup>) to EUR 19 587 million corresponding to 98% of the overall ceiling.

The detailed situation relating to guarantees is set out in the six-monthly report by the Commission on guarantees covered by the general budget<sup>10</sup>.

On 19 December 2006, the Council granted a Community guarantee to the EIB against losses under loans and loan guarantees for projects outside the Community (Decision 2006/1016/EC<sup>11</sup>). The Community guarantee is restricted to 65% of the aggregate amount of credits disbursed and guarantees provided, less amounts reimbursed, plus all related sums. The maximum ceiling for EIB financing operations carried out under this mandate in 2007-2013 is EUR 27 800 million consisting of a basic ceiling of EUR 25 800 million and an optional mandate of EUR 2 000 million, the activation of which will be decided by the Council based on the outcome of the midterm review in 2010. An amount of EUR 1 898 million was signed during 2007 under this new mandate (see section 2.3 and the table in section 2.4 of the Annex).

#### **4.2. Other activities**

Interest subsidies were granted under a number of Community programmes both inside and outside EU. Most of these programmes have been completed and no longer have any impact on budgetary expenditure. Table 2.19 lists the programmes which are still under way and the amount of interest subsidy paid during the years under review.

As further detailed in section 2.11 of the Annex, in 2007 the EIB signed seven risk capital operations under the MEDA budget for a total commitment of EUR 46.5 million and 24 technical assistance operations with an overall value of EUR 17.5 million.

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<sup>7</sup> OJ L 21, 25.1.2005, p. 9.

<sup>8</sup> OJ L 21, 25.1.2005, p. 11.

<sup>9</sup> Cumulative signatures net of cancellations (including TERRA and Turkey Special Action Program).

<sup>10</sup> COM(2007) 66 and SEC(2007) 241.

<sup>11</sup> OJ L 414, 30.12.2006, p.95.