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Leveraging the next EU budget for sustainable development finance:

THE EUROPEAN FUND FOR SUSTAINABLE DEVELOPMENT PLUS (EFSD+)

MFF

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Summary

In the European Commission proposal for the next long-term budget 2021-2027 of the European Union (EU), the proposed Neighbourhood, Development and International Cooperation Instrument (NDICI) Regulation introduces an innovative unified financial architecture to crowd in private sector investment outside the EU, based on three pillars: the European Fund for Sustainable Development-plus (EFSD+), a unified budgetary guarantee - the External Action Guarantee (EAG), and financial assistance.

The EFSD+ is conceived as a flexible mechanism, but some of its features remain too sketchy. These features could be not only much better specified but also better connected to a range of important issues, such as climate objectives, gender equality and women's empowerment principles, youth focus, linkages to business environment, geographical balance, targeting of fragile and poorer countries, specification of investment windows, provision of grievance mechanisms, and addressing tax governance issues. The governance of the EFSD+ could also be much more elaborated. The current proposal delegates great power to the European Commission on shaping these questions during the implementation of the EFSD+.

Careful attention should also be given to systemic issues related to the EU architecture for investment outside the EU. This includes the place and role of the European Investment Bank (EIB) as the EU bank, unspecified in the proposed regulation. It also relates to the coherence and synergy of the EFSD+ proposal with broader reform ambitions for the EU architecture for external investment.

Building on an open and flexible system, the European Commission proposal for the EFSD+ and EAG is an important step in the right direction towards a more effective EU financial architecture. It benefits from the Multiannual Financial Framework (MFF) and NDICI momentum, an opportunity which should not be missed. The EU has an opportunity to show it can innovate in a responsive manner to changing times and increasing challenges. This requires collective efforts, within the EU, but also in partnership with multilateral institutions and initiatives, and most of all partner developing countries. Ensuring that major concerns are addressed in the NDICI Regulation should thus be a priority if the EU is to use in a timely fashion the opportunity of leveraging its next budget for more effective sustainable development finance.

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Acronyms

ACP	African Caribbean Pacific Group of States
AFD	Agence française de développement (French Agency for Development)
AfDB	African Development Bank
AfIF	Africa Investment Facility
AIF	Asia Investment Facility
AIP	Africa Investment Platform
BMGF	Bill and Melinda Gates Foundation
CIF	Caribbean Investment Facility
DAC	Development Assistance Committee
DCI	Development Cooperation Instrument
DFI	Development finance institutions
EAG	External Action Guarantee
EBRD	European Bank for Reconstruction and Development
ECDPM	European Centre for Development Policy Management
EDF11	11th European Development Fund
EEAS	European External Action Service
EFSD+	European Fund for Sustainable Development plus
EFSI	European Fund for Strategic Investment
EIB	European Investment Bank
EIP	(European) External Investment Plan
ELM	External Lending Mandate
ENI	European Neighbourhood Instrument
EU	European Union
EU-AITF	EU-Africa Infrastructure Trust Fund
EUBIP	EU Bank for external Investment and Partnership
G-TAG	Guarantee Technical Assessment Group
GFEA	Guarantee Fund for External Actions
GNI	Gross national income
HIPC	Heavily indebted poor countries
IF	Investment facilities
IFC	International Finance Corporation
IFCA	Investment Facility for Central Asia
IFI	International Financial Institution
IFP	Investment Facility for the Pacific
IPA	Instrument for Pre-Accession Assistance

KfW	German government-owned development bank
LAIF	Latin America Investment Facility
LDC	Least developed countries
LIC	Low Income Country
MDB	Multilateral Development Bank
MFF	Multiannual Financial Framework
MSME	Micro, small and medium-sized enterprises
NDICI	Neighbourhood, Development and International Cooperation Instrument
NIF	Neighbourhood Investment Facility
NIP	Neighbourhood Investment Plan
ODA	Official Development Assistance
OECD	Organisation for Economic Cooperation and Development
OECD DAC CRS	OECD Development Assistance Committee's Creditors Reporting System
PIP	Proposed Investment Programme
SDG	Sustainable Development Goals
SME	Small, medium-sized enterprises
WBIF	Western Balkans Investment Framework

1. The MFF proposal: a new framework with EFSD+ and External Action Guarantee

The Multiannual Financial Framework (MFF) 2021-2027, as proposed by the European Commission, aims to be a political budget aligned to new political priorities for the Union post-2020.[1] One of its objectives is also to be a 'smarter' budget in terms of its ability to stimulate investment and more effectively leverage private finance, within the European Union (EU) as well as outside the EU.

In terms of its external action, the proposed MFF aims "to uphold and promote the Union's values and interests worldwide", in line with notably the 2030 Agenda for Sustainable Development, the Paris Agreement on Climate Change and the Addis Ababa Action Agenda.

1.1. The NDICI principles

Most importantly, the European Commission proposes not only to significantly increase the budget for the EU external action - from €1.087 billion in 2014-2020 to €1.279 billion in 2021-2027 (in current prices). But perhaps more fundamentally to modernise and rationalise its financial architecture and instruments, merging several external financial instruments into a broad **Neighbourhood, Development and International Cooperation Instrument** (NDICI), with a financial envelope of €89.2 billion (in current prices).[2] The single instrument aims to increase the coherence between instruments, promote economies of scale and synergies between programmes, as well as contribute to the simplification of processes.[3]

The European Commission proposes to structure the single NDICI instrument around three pillars:

- **Geographic programmes**, with €68 billion for 2021-2027 (in current prices), would constitute the main funding channels for bilateral EU cooperation with partner countries. The areas of cooperation, structured around the 'five Ps' -people, prosperity, planet, peace and partnership- would cover the following geographic regions:
  (a) Neighbourhood (at least €22 billion)
  (b) Sub-Saharan Africa (at least €32 billion)
  (c) Asia and Pacific (€10 billion)
  (d) Americas and the Caribbean (€4 billion)

- **Thematic programmes** (€7 billion) would have a worldwide coverage and are meant to complement geographic programmes by supporting global and trans-regional initiatives to promote the SDGs under the following four themes:
  (a) Human rights and democracy (€1.5 billion)
  (b) Civil society organisations (€1.5 billion)
  (c) Stability and peace (€1 billion)
  (d) Global challenges (€3 billion)

[1] For analysis of the proposal, see Jones, A., Di Ciommo, M., Sayos Monras, M., Sherriff, A. and Bossuyt, J. 2018. *Aiming high or falling short? A brief analysis of the proposed future EU budget for external action.* Briefing note No.104. Maastricht: ECDPM. https://ecdpm.org/bn104

[2] See European Commission (2018), Proposal for a Regulation of the European Parliament and of the Council establishing the Neighbourhood, Development and International Cooperation Instrument, COM(2018) 460 final, 14.06.2018.

[3] For analyses on the MFF process and NDICI overall, see ECDPM https://ecdpm.org/dossiers/multiannual-financial-framework-mff/

- The **rapid response** component (€4 billion) would constitute the main funding channel for quick response capacity for crisis management, conflict prevention and peace building, strengthening resilience and linking humanitarian and development actions.

The three pillars are also complemented by a flexible crosscutting 'Emerging Challenges and Priorities Cushion' (€10.2 billion), which corresponds to the Heading 6 on external instruments to the 'Union Reserve' (Global Margin for Commitments) throughout the MFF to tackle unforeseen events and to respond to emergencies.

The Commission's proposal also includes a number of commitments for the allocation of funding under NDICI. These include notably:

- 20% of the official development assistance (ODA) under NDICI should contribute to social inclusion and human development, including gender equality and women's empowerment;
- 25% of the NDICI financial envelope should contribute to climate objectives;
- 10% of the NDICI financial envelope should be served "to addressing the root causes of irregular migration and forced displacement and to supporting migration management and governance including the protection of refugees and migrants' rights";
- at least 75% of the NDICI financial envelope must be dedicated to geographic programmes;
- indicatively, 10% of the NDICI financial envelope to the Neighbourhood countries allocated on performance-based approach.

The proposed NDICI should also contribute to the EU target of 0.20% of the EU gross national income (GNI) towards least developed countries (LDCs), and at least 92% of the funding under the NDICI should be ODA eligible under the aid definition of the Development Assistance Committee (DAC) of the Organisation for Economic Cooperation and Development (OECD).

1.2. The proposed EFSD+ and External Action Guarantee

One of the key dimensions of the European Commission proposal is to establish a new unified financial architecture to crowd in sustainable private sector investment outside the EU, based on three pillars: the European Fund for Sustainable Development-plus (EFSD+), a unified and open system of budgetary guarantee - the External Action Guarantee (EAG), and financial assistance.

The proposed types of financing under the EFSD+ are composed of grants, financial instruments (e.g. loans, guarantees, equity or quasi-equity, investments or participations, risk-sharing instruments), budgetary guarantees and blending.

The objectives of the **EFSD+** and EAG are to support investment and increase access to financing towards the achievement of the Sustainable Development Goals (SDGs), including *inter alia* for:

- sustainable and inclusive economic and social development
- socio-economic resilience
- poverty eradication
- sustainable and inclusive growth
- decent jobs creation
- promoting economic opportunities
- promoting skills development and entrepreneurship
- focusing on local companies and micro, small and medium-sized enterprises (MSMEs)

- strengthening socio-economic sectors and areas
- addressing root causes of irregular migration, fostering resilience of transit and host communities and contributing to the sustainable reintegration of migrants returning to their countries of origin
- contributing to climate action and environmental protection.

In doing so, the NDICI proposal specifies that special attention must be given to fragile and conflict countries, LDCs and heavily indebted poor countries (HIPCs).

As indicated by its name, the EFSD+ is intended to build on and expand on the current EFSD.[4] It will notably integrate all the existing geographic blending Investment Facilities (IF), including those beyond Africa and Neighbourhood (see Box 1), in the form of regional investment platforms. The rationale is to extend the scope and geographical coverage of the existing European External Investment Plan (EIP), building on the experiences of the other regional blending investment facilities of the EU, as well as on the experiences of EU budget guarantees and of the internal European Fund for Strategic Investment (EFSI) - commonly known as the Juncker Plan - which itself is proposed to be transformed into *InvestEU*.

Similarly, the proposed NDICI foresees a new unified and open framework for guarantees, the **External Action Guarantee (EAG)**, which merges and replaces the current EFSD Guarantee, the EFSD Guarantee Fund, the External Lending Mandate (ELM) available to the EIB only, and the Guarantee Fund for External Actions (GFEA), providing budgetary guarantee for all countries covered by the EFSD+. The risks covered by the EAG include not only sovereign risks, but also commercial risks.

The EFSD+ and EAG will cover all countries in the NDICI geographical regions (i.e. Neighbourhood, sub-Saharan Africa, Asia and Pacific, Americas and the Caribbean), as well as pre-accession countries under IPA financing.

The financial amount dedicated to the EFSD+ and EAG is not specified in the proposed NDICI, which only indicates that the EFSD+ and provisioning of the EAG will be financed from the proposed €68 billion financial envelope of the geographical programmes, transferred into a common provisioning fund. The European Commission, in its proposal, indicates that the EAG may guarantee operations up to €60 billion, with a provisioning rate ranging from 9% to 50%, depending on the type of operations and associated risks (with a provisioning rate set at 9% for macro-financial assistance and for budgetary guarantees covering sovereign risks).

The proposed NDICI also states that EU Member States, as well as third countries and third parties can also contribute to the EAG, provided they do not represent a larger share (i.e. over 50%) than the EU budget financing of the EAG. Their contributions can be earmarked (geographically or thematically). In the wake of Brexit this provision takes on an added significance.

The Commission proposal also foresees the possibility of the direct participation to the capital endowment of a development bank through the financial envelope of the geographical programmes.

[4] See EU Regulation 2017/1601of the European Parliament and of the Council of 26 September 2017 establishing the European Fund for Sustainable Development (EFSD), the EFSD Guarantee and the EFSD Guarantee Fund. For an overview of the evolution of EU external investment architecture, see Gavas, M. and H. Timmis. 2019. The EU's Financial Architecture for External Investment: Progress, Challenges, and Options, CGD Policy Paper 136; and for a discussion on the EFSD and EIP, see Bilal, S. and S. Große-Puppendahl. 2018a. *The European External Investment Plan: Challenges and next steps for a game changer*. ECDPM Briefing Note 102. https://ecdpm.org/bn102

Box 1: Current EU Blending facilities

Under the ESFD, there are two regional platforms:

- the *Africa Investment Platform* (AIP), formerly known as the Africa Investment Facility (AfIF), which replaced since 2014 the EU-Africa Infrastructure Trust Fund (EU-AITF)
- the *Neighbourhood Investment Platform* (NIP), formerly known as the Neighbourhood Investment Facility (NIF)

In parallel, six other EU regional blending facilities co-exists:

- the Caribbean Investment Facility (CIF)
- the Investment Facility for the Pacific (IFP)
- the Latin America Investment Facility (LAIF)
- the Asia Investment Facility (AIF)
- the Investment Facility for Central Asia (IFCA)
- the Western Balkans Investment Framework (WBIF)

Currently, the AIP, CIF and IFP are financed under the European Development Fund (EDF11), the NIP under the European Neighbourhood Instrument (ENI), the LAIF, AIF and IFCA under the Development Cooperation Instrument (DCI) and the WBIF under the Instrument for Pre-Accession Assistance (IPA). *Note that the proposed NDICI does not include pre-accession countries, covered under the Instrument for Pre-Accession Assistance.*

The EFSD+ is proposed to be managed by the Commission, which will be advised by a strategic board. The strategic board will be composed of representatives of the Commission and the EEAS, 27 EU Member States and the EIB, with the European Parliament as an observer (other relevant stakeholders can have observer status if needed). The envisaged roles of the strategic board will be to advise and support the Commission in the strategic orientations, goals and the priorities of investments, in monitoring the right balance of geographical and thematic coverage of investment windows and in ensuring overall coordination, complementarity and coherence of the regional investment platforms, and between the three pillar of the External Investment Plan (EFSD+, technical assistance and investment climate), as well as with migration and 2030 Agenda efforts.

2. Specific considerations

The purpose of this section is not to describe what the EFSD+ and EAG should best look like, but to identify elements worth considering when assessing the merits of the Commission proposal, and suggest possible extensions. The focus is first on specific considerations related to the EFSD+/EAG only. Section 3 addresses more systemic considerations also related to the EU financial architecture.

A generic remark is that the Commission proposal aims at providing the basic architecture for a more unified and open EFSD+/EAG framework, with a broad coverage. It is foreseen as a flexible instrument, able to respond to evolving needs and priorities, with the European Commission clearly in the driving seat.

2.1. Better articulating the aims: climate, women, youth, business environment...

The aims of the EFSD+ (as summarised above -Section 1.2 - and articulated in the proposed NDICI Regulation para. (34), Art. 26.1 and Annex V) are clearly framed under the *Prosperity* as an *area of intervention for global challenges*, as stipulated in Annex III (4.C) of the proposed NDICI Regulation. While this is fully justified, these could well be extended.

Proposed aims for the EFSD+ do tend to neglect the important *Planet* area (Annex III.4.B). Given the importance of **environment and climate objectives** and **sustainable energy** as areas where the EFSD+ can effectively promote sustainable investment, explicit reference in the aims of the EFSD+ to these issues could be warranted. For instance, explicit references could be made to the **Paris Agreement on Climate change**. Annex V on the priority areas of the EFSD+ operations does mention climate action and environmental protection and management, but these are not stated in para. (34) and Art.26.1. Similarly, key principles such as promoting the conservation and sustainable use and management of terrestrial and marine ecosystems and renewable natural resources are mentioned in relation to EFSD+ operations.

To be more comprehensive, aims of the EFSD+ could also refer to *People* area (Annex III.4.A), including women (e.g. women protection and empowerment), youth (**women and youth** are useful priorities for job creation and investment support), decent work (including in global value chains) and social protection (as part of the job creation agenda), education and training (linked to sustainable investment and inclusivity agenda), health (this could build on the Bill and Melinda Gates Foundation - BMGF - contribution to the capital to the current EFSD and joint BMGF-EIB proposed health-related investments under the EFSD). Migration and forced displacement (Annex III.4.A.4) are already mentioned among the aims for EFSD+.

The underlying rationale for the EFSD and EIP is also to better link investment opportunities to the **investment climate and business environment**. As stated in the European Commission Communication *Towards a more efficient financial architecture for investment outside the European Union* (12.09.2018), "Investment supported by the EU budget must also increasingly contribute to structural reform implementation" (p.3).[5] Yet, the proposed NDICI Regulation fails to stress such linkages between EFSD+ operations with structural reforms and conducive business environment.[6] This is in contrast with the EFSD Regulation, which makes explicit reference to the EU's External Investment Plan; the EFSD as a first pillar, is complemented by technical assistance as a second pillar and the improvement of the investment climate and overall policy environment as a third pillar of the EIP. This integrated approach, which underlies the EU approach, is unfortunately no longer spelt out in the NDICI Regulation, which only outlines the EFSD+.

Although the EFSD+ is implicitly enshrined in the *Prosperity* area, the NDICI proposal could explicitly mention EFSD+ operations under the EAG as a way to contribute for instance to:

- improving business environment and investment climate (Annex III.4.C.1(b)),
- business opportunities through trade (Annex III.4.C.1(c)),
- economic diversification and value addition, regional integration and sustainable green and blue economy (Annex III.4.C.1(d)),
- fostering access to digital economies (Annex III.4.C.1(e)),
- promoting sustainable consumption and production, low-carbon and circular economy (Annex III.4.C.1(f)),
- supporting food and nutrition security, and sustainable agriculture and fisheries (Annex III.4.C.2(a&c)).

[5] The Communication goes on to specify that "Investment can be a powerful instrument to drive reform and better governance in partner countries, contributing to improved conditions for inclusive economic activity by promoting more sustainable policies and regulatory frameworks, international human rights standards, including core labour standards and due diligence requirements, more conducive business environments, new business models and greater government capacity." (pp.3-4).

[6] Under the External Investment Plan, the proper articulation and synergy among the three pillars (EFSD, technical assistance, and investment climate) are a key dimension for its success. The NDICI Regulation provides an opportunity to stress and articulate such a complementarity in the context of the EFSD+. This is not clearly done though in the Commission proposal.

Overall, the aims for the EFSD+ and EAG stipulated in paragraph (34) and Art.26.1 of the NDICI proposal could potentially better reflect some of these dimensions and the broader objectives of the NDICI. Emphasis on human rights and due diligence principles could also be added.

2.2. Lack of specific targets

The proposed NDICI Regulation specifies a number of commitments for the allocation of funding to be devoted to specific themes or types of countries (e.g. 20% for social inclusion and human development, including gender equality and women's empowerment; 0.2% of EU GNI on LDCs; 25% on climate objectives; 10% to addressing the root causes of irregular migration). But **there is no specific target in the specific context of the EFSD+**. This arguably gives greater flexibility to the Commission and the EFSD+ strategic board to define (or not) specific targets at a later stage.

Yet, this is partly in contrast to the current EFSD and practice by some multilateral development banks (MDBs) and development finance institutions (DFIs).

Take for instance **climate objectives**. The current EFSD Regulation states that at least 28% of financing under the EFSD guarantee must support investment in climate action, renewable energy and resource efficiency. This is higher than the 25% target of NDICI financing to climate objectives. The European Investment Bank (EIB) has committed to at least 25% of investments to climate action and mitigation for its overall investment (it reached 28% in 2017) and to 35% by 2020 for its investments in developing countries. The European Bank for Reconstruction and Development (EBRD) has set its climate objectives commitment to 40% of its investment. In comparison**, the NDICI overall financial commitment for climate objectives of 25% is relatively low, and there is no envisaged explicit commitment for the EFSD+.** This is even in contrast to the proposed InvestEU Regulation, which foresees that the contribution of the InvestEU Programme to the 2021-2027 MFF overall 25% target of EU expenditure contributing to climate objectives should be tracked through an EU climate tracking system. No such monitoring is foreseen under the EFSD+.

The **geographical balance** under the EFSD+ is not specified beyond the fact that regional investment platforms will be financed from the respective geographical programme envelopes. As a result, it is possible that EFSD+/EAG investments can take greater prominence in some regions or countries than others. In this respect, the Commission proposal provides great flexibility in implementation, indicating only that the "The Commission shall set up investment windows for regions, specific partner countries or both, for specific sectors, or for specific projects, specific categories of final beneficiaries or both, which are to be funded by this Regulation, to be covered by the External Action Guarantee up to a fixed amount." (NDICI Art.27.7).

One of the rationales for the EIP and EFSD has been to induce MDBs/DFIs to undertake investments in more risky and difficult countries or type of projects, where in spite of the perspective of high development impact, they tend to do less. **The EFSD+ does not directly address this need to focus on poorer and more fragile and vulnerable countries**. It only indicates that "Special attention shall be given to countries identified as experiencing fragility or conflict, Least Developed Countries and heavily indebted poor countries" (NDICI Art.26.1), without specifying what this would mean in practice.[7] This is left to the Commission, with the support of the strategic board, to determine.

There is a risk that EFSD+ operations under EAG will be directed mainly at middle-income countries (MICs). An OECD survey found that blended finance mainly targets middle income countries, with 77% of the US$

[7] A similar wording is used in the EFSD Regulation; so, the proposed NDICI Regulation is in that respect not different than the current EFSD Regulation.

81 billion in private resources mobilised by public development finance between 2012 and 2015 going to MICs and only 7% to LDCs.[8] Similarly, a recent report by MDBs indicates that poorer countries accounted for less than 4% of long-term financing for private direct mobilisation by MDBs and DFIs worldwide, around 2% in the case of the EIB and 9% for the EDFI (see Table 1).[9]

While the lack of risk mitigation tools is often cited as a major obstacle to raising private investment in poorer and more fragile countries, the EFSD+/EAG could effectively partly remedy this, justifying a strong, and perhaps more explicit focus of the EFSD+ on LDCs and vulnerable countries.

Table 1: Private direct mobilisation by MDBs and DFIs in 2017 (US$, million)

	TOTAL	Low- & middle-income countries	LICs & LDCs	Africa
EIB	36776,5	4977,1	809,5	1244,4
EBRD	801,8	664,9	N/A	1
EDFI	1067,5	1067,5	99,8	324,6
Total worldwide	51997,5	19131,5	1853,9	3,714

Source: *Compiled from MDBs (2018) Mobilization of Private Finance by Multilateral Development Banks and Development Finance Institutions.*

2.3. Level of guarantee provisions

The proposed NDICI Regulation foresees that the External Action Guarantee (EAG) may guarantee EFSD+ operations up to €60 billion, with a provisioning rate ranging from 9% to 50%. The rate of 9% corresponds to the level of the current External Lending Mandate (ELM), available only to the EIB, and to current Macro Financial Assistance and Euratom loans. Accordingly, EU budget provisions need to be made to cushion calls under the EAG only at a rate of 9% of the EU's total outstanding liabilities. Similarly, the rate of provisioning at 50% of the total guarantee obligations is identical to the one under the current EFSD guarantee used to cover the risks from loans, guarantees, counter-guarantees, capital market instruments as well as any other form of funding or credit enhancement, insurance, and equity or quasi-equity participations. In this respect, the proposed NDICI Regulation only transposes the current requirements to the EFSD+ operations guaranteed under the EAG, in a unified guarantee framework.

In doing so, however, **the Commission does not propose a specific budgetary amount to be dedicated to EFSD+ operation under the EAG. Flexibility is maintained** as to the type of operations and corresponding guarantee required. To guarantee operations up to €60 billion, Commission officials have suggested that **some €10 billion to €15 billion from the proposed NDICI €68 billion geographic programme envelope would be dedicated to EFSD+ operations under the EAG**. While these are sensible estimates, they are only potential estimates, as more or less funding might be dedicated to the EFSD+/EAG, depending on the type of operations envisioned and their risk profile. This is in contrast with

[8] See Benn, J., C. Sangaré and T. Hos (2017), "Amounts Mobilised from the Private Sector by Official Development Finance Interventions: Guarantees, syndicated loans, shares in collective investment vehicles, direct investment in companies, credit lines", OECD Development Co-operation Working Papers, No. 36, OECD Publishing, Paris, https://doi.org/10.1787/8135abde-en

[9] These different shares are also a reflection of the portfolio of the MDBs. It is worth keeping in mind that EIB activities outside the EU account for only 10% of the EIB investments, and that EIB financing for private direct mobilisation in LICs and LDCs are more than eight times bigger than the combined EDFI financing in these countries (and about four times higher for Africa), as reported in Table 1.

the current EFSD Regulation, which clearly indicates not only the maximum amount of EFSD Guarantee (€1.5 billion), but also the allocation of resources from the EU budget (€350 million) and EDF11 (€400 million) for the EFSD Guarantee Fund of €750 million. Consequently, the ESFD Regulation also specified that at least €100 million from the EFSD Guarantee Fund coverage must be allocated to Neighbourhood countries and at least €400 million from the EFSD to EDF11 (i.e. ACP) countries.

It is worth noting that the EFSD Regulation had to accommodate the existing EU financial architecture and regulations: the European Neighbourhood Instrument (ENI) -financed from the EU budget- and the 11th European Development Fund (EDF11) -outside the EU budget-, and the two corresponding blending facilities, the Neighbourhood Investment Facility (NIF) and Africa Investment Facility (AfIF), whose combined resources provided €2.6 billion for the EFSD.

The proposed NDICI Regulation provides for a unified framework, both in terms of a unified guarantee framework (the EAG), and financial instrument (notably with the proposed 'budgetisation' of the EDF – bringing the EDF inside the EU budget), which accordingly offers the opportunity for greater flexibility and adaptability, including in terms of priorities and risk exposure. Yet, considerations could be given whether the NDICI Regulation should provide more specific indications with regard to the EAG and EFSD+ operations covered.

In its Communication *Towards a more efficient financial architecture for investment outside the European Union*, the European Commission foresees that through its new blended finance instruments, guarantees and other financial instruments it will be able to mobilise €500 billion in investment for the 2021-2027 period for the MFF's NDICI. This suggests that the Commission estimates that **the EFSD+ guaranteed operations of up to €60 billion would have a leverage above eight**, i.e. generating eight times more private investment (which is still a high yet reasonable estimate for operations in poorer developing countries).

2.4. Investment windows not defined

The Commission proposes to set up specific investment windows under the EFSD+/EAG, for specific regions, countries, sectors, projects or categories of beneficiaries. The choice, to be duly justified, is left to the European Commission.

This is similar to the current EFSD, where investment windows are not specified in the EFSD Regulation, but were identified after its adoption.

However, it is somewhat in contrast to the proposed Regulation on InvestEU, where four policy windows are identified, (i) sustainable infrastructure; (ii) research, innovation and digitisation; (iii) SMEs; (iv) social investment and skills, and where indicative allocation of the EU guarantee between the policy windows is specified (in an Annex).

Considerations on flexibility and adaptability would suggest that investment windows do not need to be identified a priori in the NDICI Regulation, and can be left to a later stage. Considerations on policy steering, predictability and clear priority objectives would suggest, on the contrary, that -at least some- investment windows can be pre-identified in the NDICI Regulation.

2.5. Still a European preference

It is worth noting that the EFSD Regulation contains an explicit preference for European financial institutions to take the lead for operations under the EFSD Guarantee,[10] though it does not exclude other financial institutions (which have been '7-pillar' assessed[11]) to take the lead.[12]

The proposed NDICI Regulation does not contain such a clause relative to the EFSD+ operations under the EAG.[13] However, Art.23.6 of the proposed NDICI Regulation does suggest a general preference for European institutions, which could arguably have similar effects, as it states that:

> "Financial instruments under this Regulation may take forms such as loans, guarantees, equity or quasi-equity, investments or participations, and risk-sharing instruments, *whenever possible* and in accordance with the principles laid down in Article 209(1) of the Financial Regulation *under the lead of the EIB, a multilateral European finance institution, such as the European Bank for Reconstruction and Development, or a bilateral European finance institution*, such as bilateral development banks, possibly pooled with additional other forms of financial support, both from Member States and third parties." [*emphasis added*]

Some EU Member States had previously insisted that the EFSD Guarantee be restricted to operations under the lead of a European financial institution. Giving a preference (but no exclusivity) to the European financial institutions to lead appears thus as a compromise, between those who would prefer a fully open system and those that would prefer the guarantee to benefit operations exclusively under the lead of a European financial institution. Considerations on synergies with multilateral development banks (such as IFC for instance) - to which (some) EU Member States are also shareholders, and with regional development banks – own by partner countries, would seem to also warrant opportunities for these financial institutions to take the lead for EFSD+ operations, provided they meet EU assessment requirements.

2.6. Absence of grievance and redress mechanism

Surprisingly, the NDICI Regulation contains no grievance and redress mechanism, contrary to the EFSD Regulation, which explicitly states in Art.19 that:

> "In view of possible grievances of third parties in partner countries, including communities and individuals affected by projects supported by the EFSD Guarantee, the Commission and European Union delegations shall publish on their websites direct references to the complaints mechanisms of the relevant counterparts that have concluded agreements with the Commission. The Commission shall also provide the possibility of directly receiving complaints related to the treatment of grievances by eligible counterparts. The Commission shall take that information into account in view of future cooperation with those counterparts."

[10] Art.11.2 of the EFSD Regulation notably states that "The EFSD Guarantee shall be implemented whenever possible under the lead of a European eligible counterpart in line with the criteria set out in this Regulation."

[11] For criteria for financial entities to be entrusted in EU budget implementation tasks, see the information on pillars assessment at https://ec.europa.eu/europeaid/tags/pillar-assessments_en

[12] Out of the first 12 EFSD guarantee tools selected by the EFSD Strategic Board, ten are proposals under the lead of a European financial institution (in these cases the EIB, EBRD, EDFI, AFD, KfW, FMO and AECID), and two are under the lead of a non-European financial institution, in both cases the African Development Bank (AfDB).

[13] Article 27 of the proposed NDICI Regulation on "Eligibility and selection of operations and counterparts" does not include wording identical or similar to Art.11.2 of the EFSD Regulation.

Establishing a complaints mechanism has been a strong demand of the European Parliament and civil society organisations during the EFSD legislative process. It is also a recurrent issue raised by civil society actors on the role and activities of MDBs and DFIs.

The inclusion of a grievance and redress mechanism clause in the NDICI Regulation, at least for the EFSD+, could thus be a legitimate addition.

2.7. No provision to address tax avoidance and tax havens

The NDICI Regulation does not directly address the issue of tax avoidance, tax evasion, tax havens, illicit financial flows, money laundering which some EFSD+ operations under the EAG could possibly contribute to.

These have been an issue of concern for civil society organisations[14] and the European Parliament.

This is in contrast to the EFSD Regulation, which states (para.37) that "Financing and investment operations supported by the EFSD should adhere to the Union policy on non-cooperative jurisdictions for tax purposes", and Art.22.1 on excluded activities and non-cooperative jurisdictions, which specifies that:

> "In their financing and investment operations, the eligible counterparts shall comply with applicable Union law and agreed international and Union standards and, therefore, shall *not support projects under this Regulation that contribute to money laundering, terrorism financing, tax avoidance, tax fraud and tax evasion*.
> In addition, the eligible counterparts shall not enter into new or renewed operations with entities incorporated or established in jurisdictions listed under the relevant Union policy on non-cooperative jurisdictions, or that are identified as high risk third countries pursuant to Article 9(2) of Directive (EU) 2015/849 of the European Parliament and of the Council, or that do not effectively comply with Union or internationally agreed *tax standards on transparency and exchange of information*." [*emphasis added*]

Arguably, such basic principle-based tax-related provisions are already included in the EU Financial Regulation[15], and therefore do not need to be restated. Yet, given the these are most pertinent issues for the EFSD+, they could be explicitly referred to in the NDICI Regulation.

2.8. Governance of the EFSD+

The governance of the EFSD+ is described in a very succinct manner in Annex VI of the proposed NDICI Regulation. [16]The EFSD+ will be managed by the European Commission. The Strategic Board of the EFSD+ will in essence advice and support the European Commission, who is in the driving seat. Regional operational boards will support the Commission in the management of the regional investment platforms.

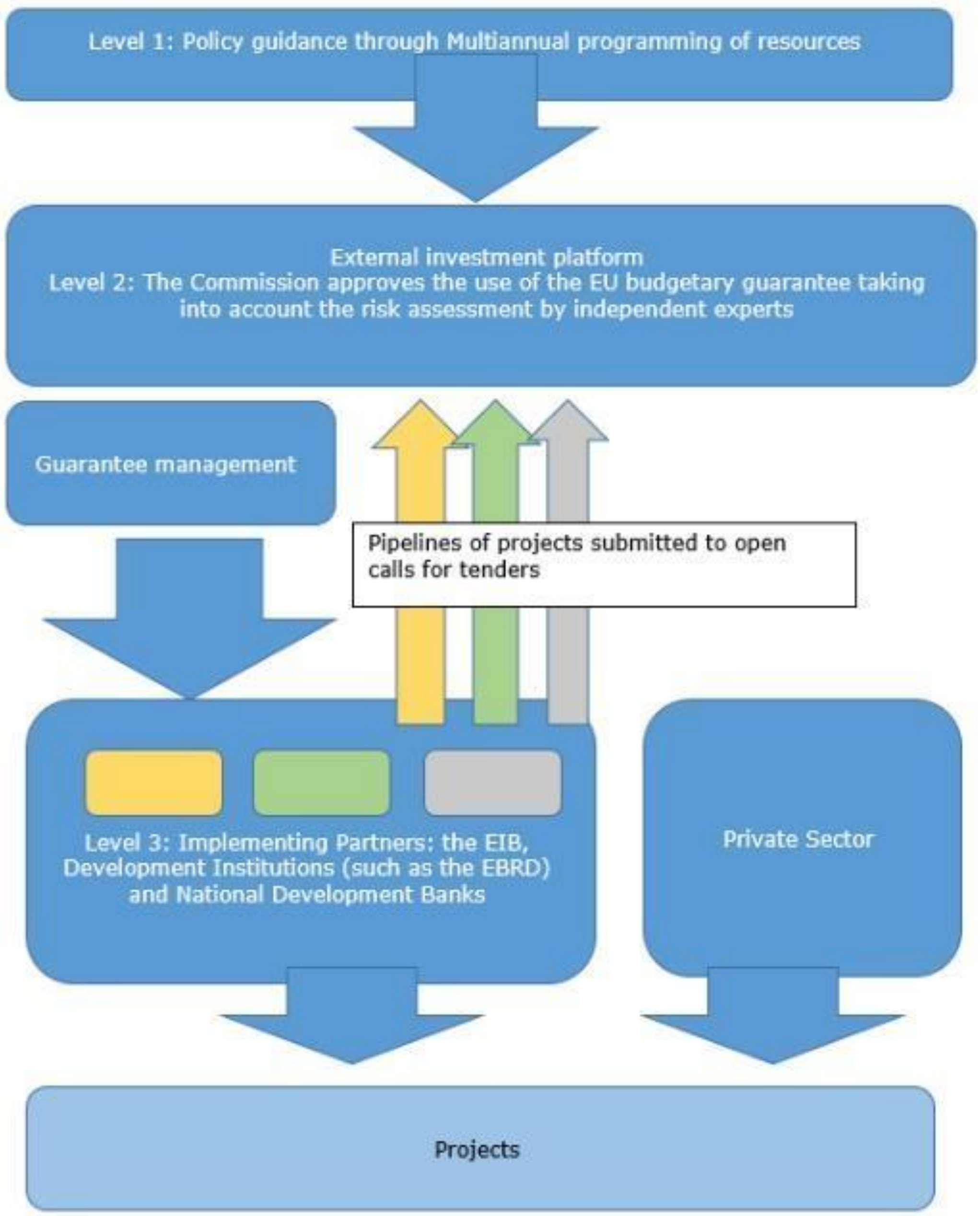
[14] See for instance the recent report by CounterBalance (2018), *Leading by example on responsible taxation*. http://www.counter-balance.org/eibtax2018/

[15] See Article 155.2 of the Regulation (EU, Euratom) 2018/1046 of the European Parliament and of the Council of 18 July 2018 on the financial rules applicable to the general budget of the Union.

[16] For wider issues associated with the governance of the NDICI overall see, Jones, A., De Groof, E. and Kahiluoto, J. 2018. *Governing a new broad instrument for EU external action: The ins and outs of the institutional power struggle.* Briefing note No.107. Maastricht: ECDPM. https://ecdpm.org/bn107

The European Commission has outlined its vision and ambitions in its Communication *Towards a more efficient financial architecture for investment outside the European Union*, where it outlines its key role in steering and managing what it calls a reinforced EU's external investment architecture (see Figure 1).

Figure 1: Architecture for the EU's external investment



Source: European Commission (2018) *Communication Towards a more efficient financial architecture for investment outside the European Union.*

In essence, the European Commission is at the centre of the External Investment Platform, which in the context of the NDICI is the EFSD+. The Commission will manage the Guarantee, following EU policy guidance (level 1) as well as advice from the Strategic Board of the EFSD+, and support from technical expertise.

The proposal from the Commission raises six possible concerns on the governance of the EFSD+ that could be explicitly address in the NDICI Regulation: (i) lack of specificity in the governance architecture, (ii) the centrality of power in the hands of the European Commission, (iii) the limited internal capacity of the Commission to deliver, (iv) the need for independent banking-related expertise, (v) the need for an explicit coordination process for EU MDBs/DFIs, and (vi) the lack of specific reporting and monitoring mechanism.

(i) Lack of specificity in the EFSD+ governance architecture:

Different types of governance models are possible, yet Annex VI of the proposed NDICI Regulation only sketch it in broad terms, lacking specificity, relating to the precise decision-making process, the types and roles of technical (financial and developmental) expertise,[17] the place of banking input, etc. The governance of the EFSD+ could be aligned to the current governance mechanisms of the EU blending facilities, or of the EFSD (with its Guarantee Technical Assessment Group (G-TAG) for instance), or based on other modalities.

The advantage of the current proposal is that by leaving governance details out of the NDICI Regulation, it provides the flexibility needed for learning from current experiences (notably on the effectiveness of the governance structure of the EFSD) and for adjusting the governance modalities of the EFSD+ as needed in the future. The disadvantage is that at this stage, it increases the level of uncertainty on the effective modalities of management for the implementation of the EFSD+, and it precludes the EU Members States and the European Parliament to shape it at the legislative level. Apparently, some EU Member States have already indicated their disagreement with the light governance modalities mentioned in Annex VI.

(ii) The centrality of power in the hands of the European Commission:

The proposed design for the governance of the EFSD+, combined with the lack of details in its modalities, to be adopted at a later stage, outside the NDICI regulation, gives de facto central authority and power to the European Commission. The centrality of the European Commission is at the heart of the EFSD+ proposal (and arguably the NDICI and MFF proposals), allegedly to provide greater flexibility, adaptability and responsiveness of the European Commission to evolving needs. The proposal also gives power to the European Commission to adopt delegated act (Art.34), including "to supplement or amend the priority areas in Annex V and the governance of the EFSD+ in Annex VI" (Art.27.9), as well as "to amend Annex VII to review or complement the [list of key performance] indicators where considered necessary and to supplement this Regulation with provisions on the establishment of a monitoring and evaluation framework" (Art.31.9). The question is whether the proposed NDICI Regulation, as currently formulated, gives or delegates too much authority and power to the European Commission in the structure and management of the EFSD+. Several EU Member States and members of the European Parliament tend to think so, and that use of delegated act should be constraints. The Strategic Board of the EFSD+ could be given explicit decision-making power, not only advisory, and this could be extended beyond strategic issues, to include individual programmes. Moreover, observer status could be given to partner (financial) institutions as well.

(iii) The capacity of the European Commission to deliver:

The EFSD+ proposal rests on the willingness and capacity of the Commission to properly structure, manage and implement the whole process, as outlined in Figure 1. This requires proper internal capacity, including in terms of banking and financial expertise, which commonly rests with the MDBs/DFIs rather than the Commission. The European Commission has demonstrated its capacity to set up the current EFSD, steer

[17] In its Communication *Towards a more efficient financial architecture for investment outside the European Union,* the Commission proposes a risk assessment group, and recognises that different models of composition and governance for such a group are possible.

the policy process and manage the selection process of proposed investment programmes (PIPs).[18] Yet, with the EFSD still being in its infancy, some concerns have been raised about the in-house expertise and capacity of the Commission to effectively manage and control the EFSD+ framework, as the Commission is not a development bank. The successful implementation of the EFSD+ will thus depend on the ability of (and support to) the European Commission to effectively mobilise the specific human resources needed, internally and externally, in synergy with other actors, to ensure quality and timely delivery of the EFSD+.

(iv) The need for independent banking expertise:

Related to the issue of the internal capacity of the Commission is the need to draw on the best available expertise in the banking-related assessment of the proposals to be covered by the EAG, including in terms of risk assessment, which requires strong financial and banking expertise. Hence the need to call on banking expertise outside the European Commission. The EIB, as the EU bank, is well-equipped to perform this task, given its expertise and experience. But the EIB is also a potential beneficiary of the EFSD+/EAG, and thus possibly not neutral enough to manage this process, being perceived as being both 'judge and party'. Arguably, such perceived conflict of interests could be managed in a structural way, insulating EIB's own origination of programmes from its risk management services to the EFSD+. Nonetheless, the perception of potential conflict of interest is likely to persist in situations where the EIB would compete with other DFIs/MDBs to get its proposed investment programmes guaranteed under the EFSD+. A further remedy could thus be to rely on the EIB banking expertise to assess only non-EIB proposals under the EFSD+, alleviating some of the perceived conflict of interest.

Alternatives could include:

- calling on a pool of experts from different EU MDBs/DFIs (and not a single DFI alone), in a more structural basis; though the potential conflict of interest could be diluted, it would arguably potentially stilly present, as DFIs/MDBs would be judge and party; or
- rely on banking consultancy not related to involved MDBs/DFIs.

Expertise on development finance is important though, as the banking-related assessment of EFSD+ proposals should be carried out in conjunction with development impact and market-based assessment, to ensure effective additionality and crowding in (and avoid crowding out) private finance, addressing clear market-failures and not adding market distortions. Such a process should also draw on a proper assessment of the experiences from the EFSD and its G-TAG mechanism, before adopting a new structure for the EFSD+.

(v) An explicit coordination process for EU MDBs/DFIs:

The NDICI Regulation does not foresee any specific mechanism or process to strengthen the coherence, synergy and coordination among the EU MDBs/DFIs and with the EU institutions. The EFSD+ could build on the effective added value and comparative advantage of MDBs/DFIs while stimulating policy and possibly modalities' alignment, as well as stimulating cooperation among them and with EU institutions. This explicit coordination mechanism would be critical also in terms of enhancing the expected development impact of the EFSD+. While such endeavours do not have to be spelt out in the NDICI Regulation, doing so would provide a strong political signal and practical guidance, including in terms of accountability and reporting.

[18] The EFSD guarantee has been fully allocated to 28 investment programmes, with the first guarantee agreement (for the NASIRA Risk-Sharing Facility) was signed between the European Commission and FMO (the Dutch DFI) on 18 December 2018 in Vienna at the High-Level Forum Africa-Europe. For an update, see https://ec.europa.eu/commission/eu-external-investment-plan/external-investment-plan-progress-so-far_en

(vi) Lack of specific reporting and monitoring framework for EFSD+:

Beside a generic reporting requirement, the NDICI Regulation does not specify what reporting, monitoring and evaluation principles and framework should be adopted specifically for the EFSD+. This is in contrast with the current EFSD Regulation, which in Article 16 outlines the reporting and accounting requirements. Given the transparency and accountability requirement called for to ensure the effective use of blended finance and guarantee for greater development impact, without distorting markets and competition or crowding out investment, the NDICI Regulation could further build on the current EFSD to more explicitly spell out the basic parameters of such reporting, monitoring and evaluation framework.

While all these governance-related issues could partly be addressed outside the NDICI Regulation, in follow up processes, the uncertainty and incompleteness created by the Commission proposal, arguably for the sake of flexibility and simplicity, could usefully be addressed in the Regulation itself.

3. Systemic considerations

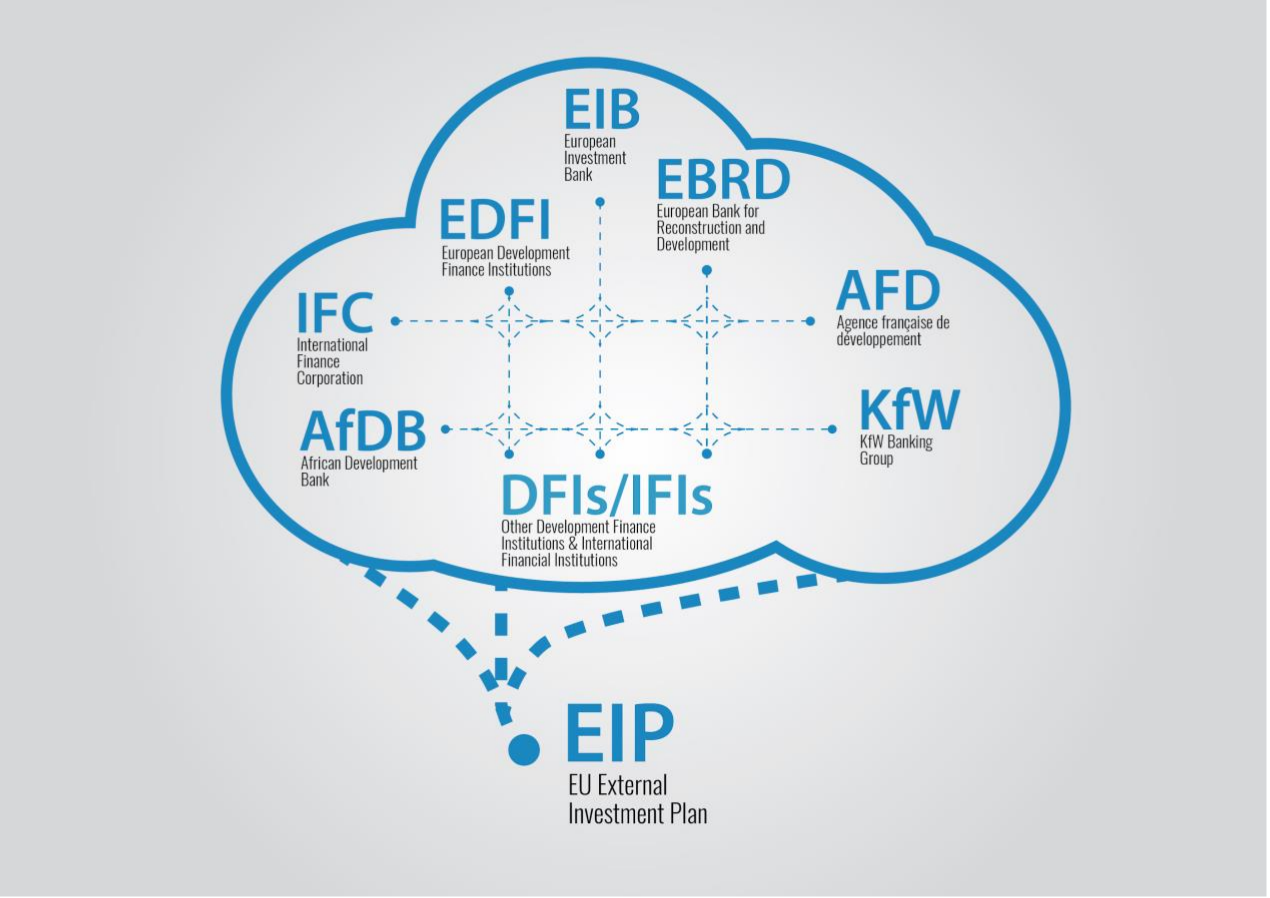
More fundamentally, the proposed EFSD+ and EAG aim at contributing to reshape the EU financial architecture for external investment. The ambition is to create a level playing field among (European) MDBs and DFIs by opening up the EU guarantees, beyond the EIB only. It is also to provide a stronger political steer to investment finance along EU development, economic and political priorities, in a flexible and responsive manner. To do so, strong power and management responsibilities are assigned to the European Commission, which becomes the steering centre -with the EIP (and proposed EFSD+/EAG) - of a European development finance architecture composed of (primarily European) MDBs and DFIs, as illustrated in Figure 2.

The Commission proposal is therefore not simply a new technical adjustment and marginal innovation to the development finance modalities of the EU, but is part of a more ambitious endeavour towards a systemic revamp of the EU financial architecture for development finance, as discussed by the Commission in its recent Communication *Towards a more efficient financial architecture for investment outside the European Union*. It is therefore also in this perspective that the Commission proposal for the NDICI Regulation, and the EFSD+/EAG must be assessed.

In considering the systemic implications of the EFSD+/EAG proposal, two issues deserve particular attention:

- the EIB and its contribution as the EU bank to EU development finance;
- the coherence and complementarity of reforms of the EU financial architecture for development finance.

Figure 2: The EIP/EFSD+/EAG steering centre of a constellation of (European) MDBs and DFIs



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3.1. What future for EIB operations?

The proposed NDICI Regulation amounts to a major reshaping of the institutional and regulatory framework under which the European Investment Bank will operate post-2020 for its activities outside the EU. This raises two questions: (i) what will be the potential consequences for the EIB? and (ii) will it enhance the overall EU financial ability to promote development investment?

The EIB operations outside the EU benefit from a sovereign risk guarantee by the EU, under the External Lending Mandate (ELM) and in the ACP countries under the ACP-EU Partnership Agreement (Cotonou Agreement), guarantee provided exclusively to the EIB and no other MDBs/DFIs. This sovereign-risks guarantee is essential for the capacity of the EIB to undertake operations outside the EU, as it allows the EIB to undertake activities in riskier countries while preserving its AAA rating and associated low financing costs on the international capital market. Without sovereign risks guarantee, the whole EIB operations outside the EU could be jeopardised.

With the Commission proposal, a unique External Action Guarantee will merge and replace the ELM, as well as the EFSD Guarantee and the EFSD Guarantee Fund. Unlike the ELM, the EAG is not limited to the EIB operations, but open to all eligible counterpart institutions, with a view to create a level playing field for (primarily European) MDBs and DFIs.

While breaking up the 'monopoly' of the EIB on EU guarantees and stimulating competition (as well as cooperation) among MDBs and DFIs is a desirable outcome, a legitimate question for the EU should be ***to which extent the EIB will be able to continue to benefit from the EU guarantee***, which is essential for the EIB to operate outside the EU.

The proposed NDICI Regulation does not provide an answer -and not even a guidance- to this question. It states that "the European Investment Bank should remain a natural partner for the Commission for the implementation of operations under the External Action Guarantee" (para. 33), but it fails to specify how. What will it mean in practice for the EIB to be a natural partner of the Commission?

Concretely, under the NDICI proposal, and in the absence of other guarantee mechanisms such as the ELM, only the EIB operations conducted under the EFSD+ will benefit from the External Action Guarantee.

In parallel, the Cotonou Agreement is also up for renegotiation, creating further uncertainty about the specific role of the EIB in the ACP under this special arrangement. Arguably, sovereign guarantee provisions could still be provided under a post-2020 new ACP/AU-EU Partnership Agreement, exclusively to the EIB or extended to some other MDBs/DFIs. However, at this stage this appears unlikely. First, the EU *Negotiating directives for a Partnership Agreement between the European Union and its Member States of the one part, and with countries of the African, Caribbean and Pacific Group of States of the other part* (21.06.2018) do not mention any such possibility; they do not even address the future of the ACP Investment Facility, a revolving fund managed by the EIB[19]. Second, it would run against the proposed NDICI logic to provide a unified guarantee mechanism with the External Action Guarantee.

As a result, the current NDICI proposal leaves the EIB in a limbo, creating unwarranted uncertainty as to the future of its operations. The lack of clarity (or embodied flexibility) in the Commission proposal only increases this uncertainty. As no guidance is provided on the final structure of the EFSD+ and type of investment windows, it is not possible, under the current proposal, to anticipate how the EIB will best fit this new framework.

If the EFSD+ is structured in a way similar to the current EFSD, with few specific thematic investment windows and call for proposals, this would likely lead to an increased fragmentation and significant diminution of the EIB activities outside the EU. This is because the EIB may no longer be able to provide comprehensive support programmes as for instance with the Economic Resilience Initiative under the External Lending Mandate,[20] and the ACP Investment Facility under the Cotonou Agreement. If the EFSD+ cannot accommodate medium- to long-term significant engagements of the EIB, this could lead to a loss of operations as well as strategic attention of the EIB for activities outside the EU, significantly reducing its development impact, with the EIB focusing instead its limited human resources and efforts to operations inside the EU.

Unlike other major European bilateral financial institutions such as the Agence francaise de développment (AFD) and the German KfW, which benefit from their respective national state guarantees, the EIB depends on the EU for sovereign guarantees. European DFIs also benefit *de facto* from a guarantee from their own

[19] See for instance Bilal, S., Große-Puppendahl, S. 2016. The EIB's innovative role in ACP countries under the Cotonou Agreement: Options beyond 2020. ECDPM Discussion Paper 196. http://ecdpm.org/dp196

[20] The Economic Resilience Initiative is a €6 billion initiative launched in 2016, aimed at upgrading social and economic infrastructure and stimulating private sector growth and job creation in the Southern Neighbourhood and Western Balkans, which will bring the total commitment of EIB operations to these Neighbourhood regions to €15 billion by 2020.

national government, which is also their shareholder. In that respect, there is no real level playing field between these institutions and the EIB, as the guarantee for the EIB is provided solely by the EU.

A reduction of EIB operations outside the EU could have a large impact on the EU external financial architecture. First, as shown in Table 2, the EIB is one of the major European financial institutions active outside the EU. But unlike the AFD or the EBRD, most of its investment operations (about 90%) are within the EU. It is also one of the lead European financial institutions when it comes to supporting and leveraging private investment, compared to other European DFIs (see Table A1 and Table A2 in the Annex). Second, the EIB accounts for a third of ODA from EU institutions (34% in 2016)[21], and as such is part of the EU institutions arsenal and capacity to act as a political actor with significant clout on the international development scene.

Recent developments have rather pointed to means for the EIB to do more outside the EU, not less, including to address the root causes of migration. For instance, the ELM for the 2014-2020 period had been increased in 2016 from €27 billion to €32.3 billion; the Impact Financing Envelope of the ACP Investment Facility had been increased by 60% (from €500 million to €800 million) and transformed into a revolving fund; the EIP and the EFSD initiative was meant to enhance the capacity of the EIB to promote more impactful investment outside the EU, not to substitute for its current activities; and the EIB President proposed at the end of 2017 to set up an EIB's subsidiary, the EU Bank for external Investment and Partnership (EUBIP), to more effectively stimulate investment outside the EU.

Table 2: Annual new committed investment in 2017 (€ billion)

	Outside Europe	**Share of total for the Group**	**Group Total**
EIB	**7.9**	**10%**	**78.2**
EBRD	**6.4**	**66%**	**9.7**
KfW	**8.2**	**11%**	**76.5**
AFD	**8.8**	**85%**	**10.4**
EDFI	**7.1**	**99%**	**7.2**
TOTAL	***38.4***	***21%***	***182.0***

Source: Compiled from annual financial statements and overviews from these MDBs

The EFSD+ and EAG could be set up in a way to better accommodate the EIB long-term strategic ambitions to be even more impactful in enhancing investment outside the EU. For instance, **a specific share of the EFSD+ operations guaranteed under the EAG up to €60 billion could be devoted to the EIB**. Alternatively, the EIB could be allowed to make major proposals, outside specific EFSD+ investment windows (or crossing over several thematic investment windows and/or over several regional investment platforms), so as to allow for innovative EIB initiatives (e.g. inspired from the Economic Resilience Initiative, or revolving funds like the ACP Investment Facility, possibly with broader geographical coverage). Or the

[21] Taking into account the EBRD in ODA from EU institutions, the share of the EIB would be at 26%. Own calculations from the OECD DAC CRS (OECD Development Assistance Committee's Creditors Reporting System) for the year 2016 (http://www.oecd.org/development/stats/idsonline.htm).

current ELM system could co-exist alongside an EAG, as currently the case with the EFSD Guarantee alongside the ELM. Provisions could also be introduced in the NDICI Regulation to allow for the continuation of the ACP Investment Facility for the 2021-2027 period of the MFF, and its possible replenishment and geographical extension.[22] More generally, the possibility of a loss of guarantee and subsidies for the EIB could also jeopardise the continuity of EIB current operations outside the EU, an issue that also deserve proper consideration.

While the proposed NDICI Regulation does not preclude such tailored made approaches for the EIB, it does not foresee any, which are left to the appreciation of the European Commission. The Council (with EU Member States also being shareholders of the EIB) and the European Parliament, together with the European Commission, could remedy this situation by jointly agreeing, in consultation with the EIB, to concrete provisions relative to the EIB under the NDICI Regulation.

In this context, it is also important to briefly point to the political economy dynamics surrounding the revision of the EU financial architecture. In essence, this has been characterised by increasing tensions between the European Commission and the EIB, with the European Commission seeking to better harness the EIB activities to its policy objectives.[23] Recurrent critics are that the EIB tends be to too conservative and risk-averse, focusing more on its investment banking perspective than on development impact objectives.

In this regard, it is important to note that the EIB has no independent power: as the 'EU Bank', it responds to the will and decision of its shareholders, the EU Member States. The EIB is thus in principle the most appropriate EU institution to finance external investment in line with EU policies and interests. Should the EIB need to act differently, and undertake significant improvements in its activities, these can be shaped and guided by the EU Member States. The proposal to set up a subsidiary of the EIB as its development arm, currently referred to as the EU Bank for external Investment and Partnership (EUBIP), is another illustration of the EU and its Member States capacity to shape and control the EIB's future activities. As the EU bank, there is institutionally no reason for a divergence of the EIB with EU policy guidance and objectives, and rivalry with the European Commission.

3.2. Towards a coherent EU architecture for development finance?

The EFSD+ and EAG are part of a larger endeavour to reshape the EU development finance in the context of the 2030 Agenda and the Addis Ababa Action Agenda on Financing for Development.[24] As outlined in the European Commission Communication *Towards a more efficient financial architecture for investment outside the European Union* (p.1), "Due to the current fragmentation, investment decisions are not always made in full coordination and consultation across institutions and Member States, thereby potentially

[22] As a revolving fund, which is now financial sustainable, additional financing from the EU budget is not necessary, though it could be envisaged to extend the activities of the Facility.

[23] Although the EIB operations outside the EU are carried under a mandate from and policy objectives set by the EU, and that the European Commission has a sit in the EIB's Board of Directors (which is responsible for approving all EIB financing operations), it is common for the European Commission to criticise EIB operations outside the EU as not sufficiently development oriented. The European Commission increasingly took back control away from the EIB, as in the case of the Africa Infrastructure Trust Fund which was managed by the EIB before being transformed as the African Investment Facility managed by the European Commission; the setting up of the EFSD to further open up the EU external financial architecture; and now the EFSD+ proposal taking secured EU guarantees away from the EIB; and similarly within the EU, the move away from EFSI to InvestEU under the proposed MFF. No doubt the EUBIP proposal was meant as a response by the EIB to this trend. For an illustration of the public raw between the European Commission and the EIB, see Devex, "EU institutions cross swords over future of development finance", 20.09.2018; and Devex, "Q&A: EIB President Werner Hoyer on European aid turf war, Iran, and more", 02.10.2018.

[24] See for instance Bilal, S. and S. Große-Puppendahl (2018b), Reshaping the EU 'private finance for development' landscape, ECDPM *Great Insights* magazine, Spring 2018 (volume 7, issue 2).

weakening the EU's ability to pursue its external policy objectives vis-à-vis third countries." The overarching objective of the reforms of the EU external investment should thus be to foster greater coherence and complementarity of the EU actions and financial instruments, at the Union and Member State levels. This is also the objective of the June 2018 Franco-German initiative "to set up swiftly a High-level group of "wise persons" on the European Financial architecture for development (especially regarding the respective roles of EIB and EBRD)"[25], currently set up by the Council.

The main issue at stake is how the EFSD+ proposal can bring the EU closer to a more effective financial architecture, and whether it opens new avenues or closes some others. This raises issues of sequencing as well as clear identification of the chosen direction.

The European Commission argues in its Communication on the financial architecture that "time is of the essence and that the EU's current focus must be on operational and practical solutions, rather than measures that would require fundamental institutional and structural changes such as the creation of new bodies or entities or mobilising additional capital participation from the EU budget" (p.2). The MFF process clearly offers not only a timely window of opportunity, but also generates the attention and dynamics needed to stimulate reforms. Yet, a comprehensive, coherent approach is needed, as competing models may otherwise have difficulties to co-exist and undermine one another's effectiveness. Strategic choices will have to be made.

This is well illustrated by the issue on the role and place of the EIB in the new architecture, as discussed in Section 3.1. Should there be a new European Development Bank or entity, such as the EIB's proposal for the EUBIP, or a merger or rapprochement between the EIB and the EBRD, or even closer structured cooperation among European MDBs/DFIs under specific institutional arrangements, these would have strong bearing on the desirable features of the EFSD+ and an EAG. The effectiveness of the EU external finance architecture will depend not just on the EFSD+, but how the EU set up of different frameworks, mechanisms and/or entity to stimulate development finance for external investment are articulated.

The proposed NDICI Regulation foresees the possibility of using the financial envelope of geographic programmes to contribute to the capital endowment of a development bank. So, the model of a European development bank is clearly compatible with the EFSD+ and the contribution from the EU budget. But the Commission is silent in its NDICI proposal and in its Communication on the articulation and complementarity between the EFSD+ and a European development bank or other development finance frameworks.

Similarly, while the Commission wants to stimulate a collaborative approach among European financial entities, it does not articulate how this could be done. European MDBs/DFIs have their own respective proposals and visions on this, not yet unified, which should be better elaborated, spelt out and articulated in a coherent manner.

The centrality of the European Commission in the NDICI proposal as well as in its vision for the future European financial architecture for development investment would imply a strong delegation of power from EU Member States and the European Parliament to the European Commission. Yet, alternative governance modalities could be envisaged (as discussed in Section 2.8), including by building more strongly on development finance entities and alternative financial and guarantee mechanisms and models.

[25] See the Meseberg Declaration: Renewing Europe's promises of security and prosperity, joint Franco-German declaration adopted during the Franco-German Council of Ministers, which took place 19 June 2018 in Meseberg, Germany.

For instance, the EFSD+, like the EFSD, is based on the principle of fixed budgetary allocation, with the foreseen depletion of the allocation from the financial envelope of geographic programmes. Yet, other models exist, such as revolving funds. This is the case for instance of the ACP Investment Facility managed by the EIB, where reflows from successful investments can be reinjected into new development investments, providing for an additional leverage of the initial endowment. An enhanced EFSD+ or complementary mechanism could be conceived as a fully revolving fund, which could then follow on stronger banking approach, with potentially higher leverage or less ODA-intensity, than the more traditional donors-type (blended) finance approach of the current proposal of the EFSD+.

So, while the 2021-2027 MFF process is a good opportunity to start pushing hard for quick reforms of the EU financial architecture ("time is of the essence" indeed to adapt the EU to new international realities), approaches to the EFSD+ could be reconsidered or the proposal could be fine-tuned. If this were the case, several options might be envisaged:

a. **The proposal for an EFSD+ and EAG as part of the NDICI Regulation could be simply abandoned at this stage**. The advantage might be to get time to elaborate a fully-fledged proposal to be enshrined in an independent EFSD+ Regulation (to replace the current ESFD Regulation) or to develop alternative models building on development finance entities initiatives and synergy, as in the case of a European development bank or similar mechanisms for instance. In this case, it might be desirable to keep the possibility of the participation from the EU budget to the capital endowment of such new development finance entity. The major disadvantage would be to lose the opportunity of the MFF 2021-2027 process to start effectively reshaping the EU financial architecture, using the potential leverage of the EU budget and guarantees of a more unified approach.

b. The NDICI Regulation could **foresee the possibility of an EFSD+ and EAG in broad terms only**, but leave most of its details to a future specific EFSD+/EAG Regulation. This would ensure that the NDICI Regulation would not preclude the future adoption of an EFSD+/EAG type of proposal, or the participation from the EU budget to a future European development bank or entity/mechanism. It would buy time to allow proper systemic considerations on the future EU financial architecture and tailor the details in a later Regulation that would complement the EFSD+. The disadvantage would be a potential loss of (political) momentum, the risk that there would be no decision taken in a foreseeable future, and the risk of discontinuity in current approaches under the current EIP and EFSD post-2020.

c. **More details of the EFSD+ and EAG could be identified**, including to more explicitly provide for synergy with the overall EU financial architecture for external investment, based on the roles of European development finance institutions, the EIB and/or a European development bank. These would not have to be left solely to the initiative of the European Commission, but could be shaped by the views of the EU Member States and the European Parliament, on which depends the approval of the NDICI Regulation. The advantage would be to reduce the uncertainty as to the future shape of the EFSD+ by addressing in the NDCI Regulation already some legitimate concerns with a view to improve the coherence and effectiveness of the EU financing for development. This would require a shared vision or at least some consensus on the direction of the future EU financial architecture for external investment. The potential disadvantage is that some of the flexibility of the EFSD+ could be lost, and wrong choices on the specific features of the EFSD+ and EAG might be more difficult to remedy.

As to the MFF 2021-2027 process in general, the issues around the NDICI Regulation, the EFSD+/EAG and **the future of the financial architecture for the EU external investment are not simply technical issues, but are also highly political ones**, which should be rooted in clear strategic interests and vision. **Building on an open and flexible system, the EFSD+ and EAG proposal is an important step in the right direction** towards a more effective EU financial architecture. It benefits from the MFF and NDICI momentum, an opportunity which should not be missed. The EU has an opportunity to show it can innovate in a responsive manner to changing times and increasing challenges. This requires collective efforts, within the EU, but also in partnership with multilateral institutions and initiatives, and most of all partner developing countries. **Ensuring that major concerns are addressed in the NDICI Regulation** (as suggested in the option (c) above) **should thus be a priority** if the EU is to use in a timely fashion the opportunity of leveraging its next budget for more effective sustainable development finance.

Annex: European Development Finance Institutions

Table A 1: Amounts Mobilised from the Private Sector by the European Official Development Finance Interventions (2012-2015, US$ million)

PROVIDER	**Credit lines**	**Direct investment in companies**	**Guarantees**	**Shares in CIVs**	**Syndicated loans**	**Grand Total**
EIB	12857, 7		150			13007, 7
EBRD		666, 4	433, 6	683	2704, 2	4487, 3
European countries						
CDC Group Plc (UK)				3430, 5		3430, 5
KfW (DE)	1356, 3	181, 1	30	357, 9		1925, 3
IFU (DK)		1140, 8	2, 1	647, 6		1790, 5
AFD (F)	438, 9		1220, 4			1659, 3
FMO (NL)			90, 2		1017, 2	1107, 3
Proparco (F)	238, 8		10, 7	726, 6	130, 7	1106, 8
Sida (SE)			894, 3			894, 3
Norfund (NO)	25, 5	344, 6		126, 3		496, 5
SIFEM (CH)		3		223, 8	5, 5	232, 3
Finnfund (FI)		152, 5		68, 1	2, 7	223, 3
DFID/DECC (UK)				138, 9		138, 9
BIO (BE)	54	19, 8		3, 7	21, 1	98, 5
Swedfund (SE)		5		48, 5	5, 2	58, 7
DECC (UK)				57, 5		57, 5
MAEC FONPRODE (ES)				51, 2		51, 2
DFID (UK)				45, 2		45, 2
SOFID (PT)		3, 9	21, 3			25, 2
MFA (LU)				13, 9		13, 9
OeEB (AT)				1, 8	1, 2	3
Camoes Institute (PT)			0, 5			0, 5
TOTAL EUROPE	**14971, 3**	**2517, 2**	**2853**	**6624, 5**	**3887, 7**	**30853, 7**
(as % of total world)	*98*	*54*	*8*	*70*	*25*	*38*

Source: Compiled from Benn, J., C. Sangaré and T. Hos (2017), "Amounts Mobilised from the Private Sector by Official Development Finance Interventions: Guarantees, syndicated loans, shares in collective investment vehicles, direct investment in companies, credit lines", OECD Development Co-operation Working Papers, No. 36, OECD Publishing, Paris, https://doi.org/10.1787/8135abde-en

Table A 2: Profile of EDFI member institutions, 2015

	Investments (€, million)			**Financial instruments** (%)			**Technical assistance** (€, million)
	Annual commitment	**Portfolio**	**Investment funds**	**(Quasi)equity**	**Loans**	**Guarantees**	**TA**
BIO (BE)	168	715	200	35	65	0	0,4
BMI-SBI (BE)	8	37	0	99	1	0	0
CDC (UK)	1162	6920	3618	78	16	6	1,4
COFIDES (ES)	165	881	88	44	56	0	0
DEG (DE)	1533	7247	1632	35	65	0	4,1
FINNFUND (FI)	188	719	126	50	50	0	5,4
FMO (NL)	1837	9155	432	42	56	2	6,4
IFU (DK)	147	669	114	64	35	1	0
NORFUND (NO)	357	2078	297	86	13	1	1,0
OeEB (AT)	229	1079	300	30	63	8	1,0
PROPARCO (F)	1129	5656	689	23	75	2	0,8
SIFEM (CH)	73	632	568	82	18	0	0
SIMEST (IT)	154	963	0	73	27	0	0
SOFID (PT)	2	10	0	0	65	35	0
SWEDFUND (SE)	64	465	148	54	46	0	0,4
TOTAL	7216	37224	8212				20,8

Source: Compiled by the author from EDFI (2016), Investing to create jobs, boost growth and fight poverty.

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