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COVER NOTE

From:	Secretary-General of the European Commission, signed by Mr Jordi AYET PUIGARNAU, Director
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To:	Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of the European Union
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Subject:	COMMISSION DELEGATED DECISION (EU) .../... of 15.4.2016 amending Annex III to Decision No 466/2014/EU of the European Parliament and of the Council granting an EU guarantee to the European Investment Bank against losses under financing operations supporting investment projects outside the Union, as regards Belarus

Delegations will find attached document C(2016) 2164 final.

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COMMISSION DELEGATED DECISION (EU) .../...

of 15.4.2016

amending Annex III to Decision No 466/2014/EU of the European Parliament and of the Council granting an EU guarantee to the European Investment Bank against losses under financing operations supporting investment projects outside the Union, as regards Belarus

EXPLANATORY MEMORANDUM

1. CONTEXT OF THE DELEGATED ACT

In January 2015, COREPER endorsed a list of 29 measures to enhance the EU's policy of critical engagement with Belarus. One of these measures concerns the review by the EU of its restrictive approach to European Investment Bank (EIB) lending (Belarus is currently not eligible for the EU guarantee under the so-called external lending mandate of the EIB for 2014-2020, granted by a decision of the European Parliament and the Council¹). This measure was particularly highlighted in the conclusions of the Political and Security Committee of 1 October 2015².

In its conclusions of 15 February 2016, the Council decided to accelerate the implementation of measures which aim at enhancing the EU-Belarus cooperation in certain economic, trade and assistance-related areas, notably as regards cooperation with International Financial Institutions, in particular the EIB and the European Bank for Reconstruction and Development (EBRD). The Council also encouraged Belarus to accelerate its economic reforms as well as to ensure respect of fundamental freedoms, rule of law and human rights.

As part of the 29 measures endorsed by the Council, the Commission and the EEAS have been working closely together on the political, economic, social and environmental assessments of the current situation in Belarus. These assessments conclude that there is sufficient ground for a relaxation of the EU's restrictive approach to Belarus by making Belarus eligible for EIB financing under the EU guarantee.

Annex II to Decision No 466/2014/EU, setting out the list of countries potentially eligible for EIB financing under EU guarantee, includes Belarus. According to Article 4(2) of Decision No 466/2014, the Commission is empowered to adopt delegated acts concerning amendments to Annex III which sets out the list of eligible countries. In line with the EU policy and strategy towards Belarus and taking into account the overall economic, social, environmental and political context, as well as the relevant Council conclusions, Belarus should be added to Annex III, making EIB financing operations in Belarus eligible for EU guarantee coverage.

2. CONSULTATIONS PRIOR TO THE ADOPTION OF THE ACT

Political context

Internally, Belarus remains a centralised and autocratic state, tightly controlled by the President. President Lukashenka was re-elected on 11 October 2015 with – according to the Belarusian Central Elections Committee – 83.5% of the vote. Although elections were conducted in a peaceful atmosphere and a number of unsanctioned demonstrations were allowed to take place, significant problems, particularly during counting and tabulation undermined the integrity of the elections. The human rights and democracy situation also

¹ Decision No 466/2014/EU of the European Parliament and of the Council of 16 April 2014 granting an EU guarantee to the European Investment Bank against losses under financing operations supporting investment projects outside the Union, OJ L 135, 8.5.2014, p. 1 ("Decision No 466/2014").

² CFSP/SEC/0659/15

remain of serious concern, especially concerning freedom of assembly and association, and freedom of speech/media. Belarus remains the only country in Europe where the death penalty is applied.

However, over the two last years there has been progress. The decrease of tensions was triggered by a more pro-active participation of Belarus in the Eastern Partnership, the start of negotiations on a Visa Facilitation and Readmission Agreement, the conclusion of negotiations on a Mobility Partnership, the start of the EU-Belarus Interim Phase on Modernisation Issues, the joining by Belarus of the Bologna process, the signing of a Memorandum of Understanding for cooperation on energy security, and the participation by Belarus in the latest UN Universal Periodic human rights review, where Belarus accepted 168 out of 259 recommendations. Belarusian authorities notably agreed to carry out events in order to discuss a moratorium on the death penalty. In addition, upon Belarusian initiative, in July 2015 the EU and Belarus resumed the Human Rights Dialogue, and on 22 August 2015 the remaining political prisoners were released.

The regional context has also changed as the result of the crisis in Ukraine. Belarus has so far taken a constructive stance by hosting peace negotiations resulting in the Minsk Agreements. Belarus resisted Russian pressure to introduce restrictive measures against Ukraine, never recognised the annexation of Crimea, and did not suspend the Commonwealth of Independent States Free Trade Area obligations towards Ukraine. Belarus has rather reiterated the importance it attaches to Ukraine's territorial integrity and increased trade with Ukraine.

On 15 February 2016, the Council decided that the EU will not extend the restrictive measures for 170 individuals and three companies³. The Council further decided that the arms embargo and the restrictive measures related to the four individuals listed in connection with the unresolved disappearances of two opposition politicians, one businessman and one journalist will be extended for a period of twelve months. At the same time the Council decided to accelerate the implementation of measures aimed at enhancing EU-Belarus cooperation in a number of economic, trade and assistance related fields, with the goal of modernising Belarus and its economy and for the benefit of the Belarusian population, including in view of WTO accession and in cooperation with International Financial Institutions, in particular the EIB and the EBRD in line with their respective mandates.

If the positive trend continues, in time, this could lead to the negotiation of a new legal framework putting Belarus at an equal footing with the other Eastern Partnership countries.

In summary, against the backdrop of this assessment and based on the Council conclusions of 15 February 2016, the EU should no longer exclude Belarus from access to EIB financing in the context of the Decision No 466/2014.

Economic and social assessment

After a strong performance during the 15 years that preceded the 2009 global crisis, Belarus's macroeconomic situation has deteriorated significantly, mainly reflecting structural constraints related to a growth model in which the private sector and market signals continue to play an insufficient role. With this model hampering the efficient allocation of resources and limiting productivity growth, attempts to boost growth by easing macroeconomic policies, including wage policy, have tended to generate balance of payments and inflation pressures.

³ Foreign Affairs Council - 15/2/2016 - Conclusions on Belarus - 6052/16 COEST 30

The authorities have, however, responded to the last three episodes of balance of payments crisis or fragility with appropriate adjustment measures that have managed to restore macroeconomic stability. They have also been taking measures to increase the degree of market orientation of their economy, although so far the approach has been very gradualist and shy, aiming to restore economic stability and growth by amending the existing system rather than by moving decisively towards a full-fledged market economy model. A more decisive approach to systemic economic transformation would therefore seem important.

Following three years of modest economic growth (below 2% per annum), Belarus entered recession in 2015, for the first time in the last 20 years, and its real GDP is estimated to have declined by 3.9%. Although recession was largely a result of external shocks, including a recession in Russia and Ukraine, low commodity prices and slow growth in the EU, it was also a consequence of the above-mentioned accumulated economic and structural problems.

The contraction of the economy was driven by a fall in exports, reflecting the recession in major trading partners, Russia and Ukraine, but also the tightening of monetary, fiscal and wage policy that compressed domestic demand and investment. On a positive side, tight demand policies, together with the falling economic activity, helped contain inflation in a context where the marked depreciation of the Belarussian rouble was adding upward pressure on prices (between mid-November 2014 and by mid-February 2016, the Belarussian rouble lost 51% of its value against the dollar). In addition, prudent fiscal policy safeguarded the headline budget surplus, despite the recession and the presidential elections in October last year. The national bank moved to a fully flexible exchange rate regime in June 2015, which helped protect the almost depleted foreign exchange reserves and absorb part of the external shock, leading to a significant current account adjustment (in 2015, the current account deficit is estimated to have shrank to 2% of GDP, from 6.7% of GDP in 2014 and over 10% of GDP in 2013).

The authorities have made some progress with structural reforms, albeit to a more limited extent. Although state-owned enterprises (SOEs) continue to dominate the economic structure in Belarus, including the banking system, some progress has been made with introducing of corporate governance in the SOEs by replacing the system of hard quantitative targets with indicative ones. Progress with actual privatisation of SOEs, however, has been limited, with targets announced by the authorities in previous privatisation plans having being missed. This year, the authorities are planning to move ahead with the privatization of small and medium-sized SOEs. Progress has also been made towards a more free allocation of bank credit by reducing bank lending under government programmes. Starting in February 2015, all new government directed lending is being channelled through the Development Bank, relieving somewhat commercial banks from state interference. In addition, since 2009, significant progress has been made with price liberalisation, although the process was temporarily interrupted by the introduction at the end of 2014 of a freeze in prices, aimed at limiting the inflationary impact of the depreciation of the currency. The share of administered goods in the consumer price index basket has fallen from almost 50% in 2011 to 18% in 2016, following a deregulation of all socially sensitive goods in January 2016. During last year, Belarus has also intensified its efforts to move ahead with the WTO accession negotiations.

Over the past decade, rapid economic growth contributed to a substantial reduction in poverty ratios and an improved income distribution. The absolute poverty rate declined from over 30% in 2002 to 6.3% 2012, while the Gini coefficient fell from 0.30 to 0.26 in the same period. As a result of the recession that hit Belarus last year, the unemployment rate, which has traditionally remained at low level of about 0.5% of the labour force for years partly

reflecting excess employment in state-owned enterprises, has increased moderately (to 1%) in 2015. To support the challenges of the reorientation from mostly state-run economy towards more market-based economy, Belarus will be faced with the need to develop a modern social safety net, including strengthening of its unemployment benefit and targeted social assistance schemes as well as the pension system.

The authorities are currently conducting negotiations with the IMF on a macroeconomic adjustment and structural reform programme that could be supported by an Extended Fund Facility, building also on the Road Map for Structural Reform the World Bank has recently put together in close consultation with the authorities. The EU is actively supporting both sides to come to an agreement.

In this new context, and provided the appropriate reform measures are put in place, financial support from the EU and the international community, including through the relaxation of restrictions on EIB activities in Belarus, could help the country develop its private sector, improve its infrastructure and foster productivity growth, thus contributing to improve the dynamism and medium-term growth performance of Belarussian economy.

Environmental aspects

Belarus is characterised by a low population density and wide areas of natural landscapes, forests and wetlands. Land degradation, pollution of ground and surface water, waste management, as well as radioactive contamination from the Chernobyl accident in 1986 are some of the main current environmental concerns in the country. An important new risk factor will appear as of 2018 with the launch of Astravets nuclear power plant first reactor.

Belarus is eager to approximate its environmental legislation with European standards and is the only country in the Eastern Partnership setting environment as a priority among the three bilateral cooperation sectors under the Multi-Annual Indicative Programme. Several cross-border co-operation projects are being implemented in the field of relevant programmes with Latvia, Lithuania, Poland and Ukraine, mainly in the fields of water and waste management as well as natural risk prevention (flooding, wildfires).

Sectorial dialogue on Environment with Belarus is also progressing well and is normally attended on a relatively high level from Belarus side. Current outstanding trans-boundary environment issues between EU and Belarus include biodiversity issues, air quality management, issues under Espoo Convention in relation to the Astravets Nuclear Power Plant and the management and protection of shared rivers, such as the Neman river.

On a regional level, Belarus is actively participating in Eastern Partnership Panel on Environment and Climate Change and several EU regional programmes on environment. The country has also successfully organised the First Eastern Partnership Informal Ministerial Dialogue on Environment in 2015 and is a party to several multilateral environmental agreements.

Support from the international community, such as through EIB financing that promote the application of the appropriate environmental standards, will support the environmentally sound and sustainable development of the country.

3. LEGAL ELEMENTS OF THE DELEGATED ACT

The present Commission delegated decision aims at amending Annex III of Decision 466/2014/EU by adding Belarus in the list of eligible countries for EIB financing operations with EU guarantee coverage.

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amending Annex III to Decision No 466/2014/EU of the European Parliament and of the Council granting an EU guarantee to the European Investment Bank against losses under financing operations supporting investment projects outside the Union, as regards Belarus

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Decision No 466/2014/EU of the European Parliament and of the Council of 16 April 2014 granting an EU guarantee to the European Investment Bank against losses under financing operations supporting investment projects outside the Union,⁴ and in particular Article 4(2) thereof,

Whereas:

- (1) There has been some progress in the economic, social, environmental and political areas in Belarus since the adoption of Decision No 466/2014/EU.
- (2) In January 2015, COREPER endorsed a list of 29 measures to enhance the EU's policy of critical engagement with Belarus. One of these measures concerns the review by the EU of its restrictive approach to European Investment Bank (EIB) lending in Belarus.
- (3) In its conclusions of 1 October 2015, the Political and Security Committee listed additional concrete measures to deepen the EU's policy of critical engagement with Belarus and notably the measure easing the restrictions on EIB financing in Belarus.
- (4) In its conclusions on Belarus of 15 February 2016, the Council decided to accelerate the implementation of measures aimed at enhancing EU-Belarus cooperation in a number of economic, trade and assistance related fields, with the goal of modernising Belarus and its economy and for the benefit of the Belarusian population, including in view of accession to World Trade Organisation and in cooperation with International Financial Institutions, in particular the EIB and the European Bank for Reconstruction and Development (EBRD) in line with their respective mandates. The Council also encouraged Belarus to accelerate much needed economic reforms.
- (5) Tangible steps taken by Belarus to respect universal fundamental freedoms, rule of law and human rights would remain key for the shaping of the Union's future policy towards Belarus.

⁴ OJ L 135, 8.5.2014, p. 1.

- (6) Given the political developments in Belarus, financial support from the Union and the international community, including through the relaxation of restrictions on EIB activities in Belarus, could help the country to develop its private sector, improve its infrastructure and foster productivity growth, thus contributing to improve the dynamism and medium-term growth performance of Belarussian economy. Moreover, EIB financing operations which promote the application of the appropriate environmental standards should support the environmentally sound and sustainable development of Belarus.
- (7) Therefore, the Commission, with the involvement of the European External Action Service, has assessed that the overall economic, social, environmental and political situation allows adding Belarus to Annex III of Decision No 466/2014/EU, which sets out the list of countries eligible for EIB financing under Union guarantee.
- (8) Decision No 466/2014/EU should therefore be amended accordingly,

HAS ADOPTED THIS DECISION:

Article 1

In point B(2) of Annex III to Decision No 466/2014/EU, the words 'Eastern Europe: Republic of Moldova, Ukraine' are replaced by 'Eastern Europe: Belarus, Republic of Moldova, Ukraine'.

Article 2

This Decision shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

Done at Brussels, 15.4.2016

For the Commission
The President
Jean-Claude JUNCKER