

Evaluation Report

Operations Evaluation Department (EV)

Evaluation of the impact of
EIB financing on Regional
Development in Greece

A synthesis report



European
Investment
Bank

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External Consultants:

WEIC – Dr. Julian Bharier
Dr. Dieter Havlicek

EIB:

Operations Evaluation

Bertrand Rossert
Judith Goodwin
Iris Oppermann

Economic & Financial Studies

Patrick Vanhoudt

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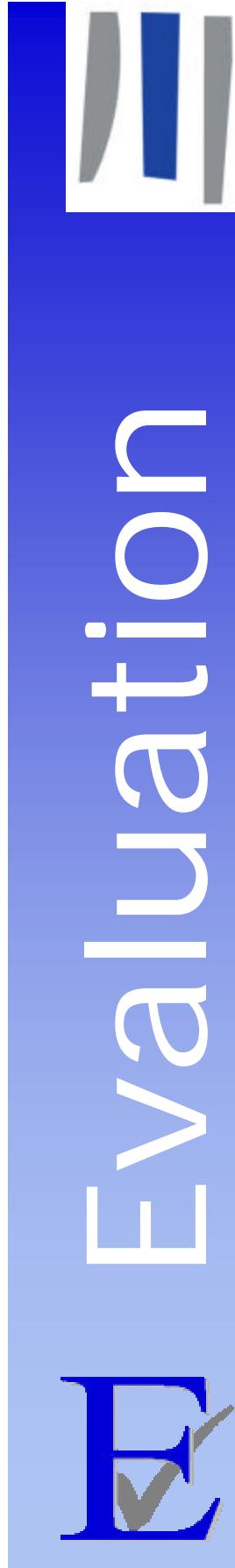


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Executive Summary

The present evaluation has assessed Greek projects financed by the Bank that were completed over the period corresponding to the first two Community Support Frameworks (CSF), i.e. 1989-2000. It therefore evaluates: 1) projects selected before the Bank started producing an annually revised medium-term Corporate Operational Plan (COP - the COP provides a tool for setting future lending priorities); 2) in the particular case of an Objective 1 country, projects selected before the Bank adopted new guidelines in 2001 to improve the appraisal of regional development projects. Some findings and recommendations also apply outside Greece, although it is beyond the scope of this evaluation to establish where and when this could be the case.

The evaluation was performed in two stages: desk reviews of 56 projects were first carried out, then visits to project sites and discussions with promoters took place for nine individual projects and two global loans (5 global loan allocations were visited). EIB investments were dominated by infrastructure projects (three large ones in particular), with industry and services only accounting for 8% of the contract amounts signed between 1989 and 2000.

Considerable modernisation has taken place in Greece in recent years with a notable development of the service sector. However, this has yet to translate into convergence of the Greek standard of living towards the EU average.

The Bank's financial impact over the last ten years has been very significant: EIB loans have been on considerably better terms than alternative sources of finance, other than the EU grants which co-financed 30 of the 56 projects evaluated. The EIB has contributed 4.4% to overall investment in Greece between 1996 and 2000, which is 2.5 times more than the EIB contributed on average in the EU. This was achieved, in particular, with the Bank establishing long-standing relationships with key promoters, especially in the public sector. The Greek authorities have supported the Bank's intervention, in particular by usually providing a State guarantee for EIB loans.

Project identification and selection strategy were appropriate in some sectors, such as electricity and telecommunications, but not in other sectors such as transport, where most lending took place. In most cases, the EIB accepted projects when and as presented by the Greek authorities. In many cases, the Bank came in late in the project cycle and often after the project had received an EC grant. This also applies to framework loans covering a large number of small projects, particularly when they were not channeled through a company but a public institution.

The period evaluated was one of very rapid lending growth for the Bank, although lending in Greece could have been higher, possibly in the electricity sector and the private sector (manufacturing and services). Lending growth and the overly long and complex processing of appraisal and Board reports may have overstretched the project appraisal resources of the EIB. Out of 56 project appraisals, 26 suffered from over-optimistic conclusions (paying insufficient attention to weak regulatory and institutional set-up or to low economic profitability) or incomplete project information

(mainly immature project designs). In a number of cases, especially in the transport sector, more consistency in cost calculation (e.g. contingencies or VAT) would have been desirable. More attention should also have been given to cost-efficiency.

The evaluation shows that there is no single unambiguous indicator of regional development and that a more qualitative and stepwise analysis is necessary. In the transport sector, the project cost or the ERR calculations were not always consistent and seven projects approved by the Bank were, at least in part, oversized. Environmental issues have been handled in a satisfactory way for all projects. Procurement procedures were appropriate whenever EU Directives were applicable (transport sector), although less consistent otherwise. Nevertheless, in the evaluators' opinion, a more rigorous approach should have led the Bank's appraisal process to reject seven to 10 of the 56 projects evaluated and, by influencing the design or the institutional set-up, to have a greater impact on about a further 16 of the projects.

The majority of Bank-financed projects had an impact on regional development and are now operating satisfactorily: 39 projects out of 56 can now be considered to have good or satisfactory outcomes, both in terms of operation success and of their individual impact on regional development (i.e. a 70% success rate), although ten projects failed substantially to achieve their overall physical objectives (including two global loans that failed to make more than one allocation). With respect to implementation delays and cost overruns, 29 projects faced substantial delays and 22 had significant cost over-runs. In addition, overall, the direct employment impact of projects, although not a prime consideration in project selection, was limited. It is beyond the scope of this evaluation to calculate the indirect employment impact.

The Bank's project monitoring was too limited in scope and depth to have an impact on project implementation, except in a few problem projects. The Bank should establish objectively verifiable indicators to detect problem projects and to implement appropriate corrective actions.

The evaluation concludes that the Bank's overall (and essentially financial) contribution to development over the last ten years in Greece was positive, although the Bank could have had a greater impact with a more systematic project identification and project appraisal discipline - particularly in the infrastructure sectors where most of the lending took place. There is one over-riding lesson to be learned from this evaluation for the future lending to accession countries eligible under Objective 1: regardless of the Bank's lending volume, it is to the ultimate benefit of the country's convergence, as well as to the whole EU economy, for the Bank to retain rigorous standards of project selection, approval and monitoring.

Recommendations

The Bank has recently proposed measures to enhance its impact on regional development. In 2001 for example, proposals were presented to the Board to improve the ex-ante assessment of the regional development impact of projects by using indicators. The technical and economic services now have software that allows consistent computation of the main parameters of an ERR calculation for transport projects and the guidelines for project cost computation have been revised. However, these measures still need implementing or enforcing.

Operations Evaluation recommends the following additional improvements:

Recommendations and response of the EIB services

	Recommendations	Comments:
1	Project selection should be based on a selection strategy designed to promote convergence (as outlined in section 4.3); it should be made known to promoters	The Bank's Corporate Operational Plan (COP) is an effort to provide for this strategy. Further refinements e.g. in terms of indicators are being developed.
2	In particular, the evaluation shows the need for a more systematic identification of lending priorities, based on country and sector analyses that should be regularly updated. For the period evaluated, sector analyses only covered energy and telecommunications. The recommendation is that they should in future cover all the main EIB lending sectors and in particular the infrastructure sectors. Eventually, they should be reflected in the structure of the portfolio.	Ops A welcomes the availability of value-adding sector studies for the individual markets in which it operates. However, the staff implications for both Ops A and PJ have to be carefully assessed.
3	The evaluation has shown cases of deficient analysis of: <ul style="list-style-type: none">• project preparation and design,• the promoter's project management skills,• the project's economic profitability and sustainability,• outstanding issues concerning asset ownership or the regulatory framework. The recommendation is that a stricter appraisal discipline should be applied, paying attention to these aspects.	These are key items for the Bank's project assessment. In order to allow for "lessons learnt", it would be useful to point out concrete shortcomings.
4	The evaluation has identified a lack of clear guidelines on how to deal with oversized projects. The recommendation is that financing oversized projects should be rejected unless the project can be redesigned and reduced to an appropriate size.	It is part of the Bank's normal appraisal process to include a project's dimension in the overall feasibility analysis.

	Recommendations	Comments:
5	The project risks and issues should always be listed in the Board reports and should fully reflect the analysis contained in the appraisal reports. Mitigating measures agreed with the promoter should be spelt out. The promoter should also be informed of the project risks and issues identified by the Bank.	In its general form, this recommendation is operational practice for OpsA and PJ project appraisal throughout the EU. Mitigants to risk would normally be addressed in contractual arrangements with promoters, who would therefore be made aware of them not later than at the time of negotiation.
6	Following the implementation of the 2001 guidelines presented to the Board, the impact of a project on regional development should be explicitly assessed at appraisal, at least through a qualitative analysis, and when possible quantified.	This recommendation has been accepted as noted in the report.
7	The evaluation has shown that EIB interventions on problem projects should be more systematic. The recommendation is to design and implement an early warning system, with objectively verifiable indicators set at appraisal, that would provide the basis for proper monitoring of projects.	This recommendation is being implemented also in projects included in the report.
8	Exit strategies should be designed to determine if and when the Bank should abandon its participation in problem projects. This could involve the transfer of the responsibility for the project to a "troubleshooting team" as an intermediate step. The recommendation is that, in any event, the promoter should be required to present a remedial action plan for the Bank's approval once the problems have been identified.	Project specific problems are addressed when the need arises and credit-specific issues also with a view to maintaining the project's and the borrower's financial viability. Already implemented (joint Ops/PJ/CRD teams).

1 Introduction

1.1 Objectives of the Evaluation

The main objectives of this evaluation are:

1. To assess the impact of the EIB's lending on regional development in Greece during the period 1989-2000 and;
2. To identify means by which this impact could have been strengthened.

The report solely concentrates on the Bank's lending on own resources, which constitutes by far its primary activity in Greece, and has excluded from its scope the EIB's subsidiary activities, for instance in relation to the European Economic Area (EEA) Financial Mechanism or the European Regional Development Funds (ERDF) or Cohesion Fund projects. As the Bank's borrowing activities in Greece were examined in a 1999 evaluation report¹, they were also left outside the scope of this evaluation.

All of Greece was eligible for regional development loans from the EIB under Objective 1 of the European Union's (EU) regional development policy² during the period under review. This is because the Greek average per capita GDP in purchasing power standards (PPS) remained less than 75% (67% in 2000³) of the joint average per capita GDP for the 15 EU Member States (EU15). Consequently, the first main objective of the evaluation is to assess the impact of the EIB's lending on the economic development of Greece.

Chapter 2 starts by comparing macroeconomic and other relevant data for Greece with the EU15 average and makes a comparison with other EU Objective 1 regions. It goes on to analyse the content and scope of the two Community Support Framework (CSF) programmes that covered the period and concludes with an overview of the EIB's project portfolio.

¹ "The impact of EIB borrowing operations on the integration of new Capital Markets" November 1999. Published on the EIB Internet site.

² EU, 'L'Europe au service du développement régional', 1996, pp. 6-7.

³ EU 'Summary of the Community SupportFramework: Greece 2000-2006', p.2.

Chapter 3 evaluates the performance of the EIB's operations in Greece over the period 1989-2000. It examines the following aspects and, where relevant, the Bank's impact on them:

- Project identification, selection and relevance
- Project costs, financing and procurement
- Project implementation and performance
- Project profitability and sustainability
- SME development through global loans
- Employment creation
- Environmental protection

Identifying the means by which the EIB's performance could have been strengthened essentially consists of assessing the project selection, implementation and monitoring processes. Chapter 4 therefore focuses on defining potential selection indicators, criteria and agreed reference points, then tests them on the projects evaluated.

The evaluation's main findings and recommendations are of relevance not only for lending in Greece, but also for lending in accession countries whose entire economies will similarly be eligible for regional development loans. In this context, we would like to stress that there have been substantial political, economic and structural developments in Greece, as well as significant changes linked to EU policies and Directives during the period under review. At the same time, the EIB has introduced new or revised lending and operational policies aimed at increasing efficiency and responsiveness to the requests of the EU Member States, other countries and project promoters.

To some extent, the findings could extend beyond projects financed in Greece to operations carried out by EIB in other EU regions, since, for instance, the project appraisal methodology is the same for all projects financed in the EU. However, it goes beyond the scope of this evaluation to establish whether and when the report findings apply outside Greece.

1.2 Methodology

The evaluation methodology developed by the EIB's Operations Evaluation Department (EV) is in line with the evaluation criteria approved by the Evaluation Cooperation Group (ECG) of the multilateral financial institutions. It covers the relevance, efficacy, efficiency, sustainability and impact of the projects; it also assesses the Bank's and the promoter's performance in relation to the project.

The evaluation was carried out in two stages. In the first stage, a ‘desk review’ was undertaken of all EIB projects in Greece completed between 1989 and 2000. This comprised a detailed examination of numerous documents relating to each of the projects, including internal project dossiers, as well as discussions with EIB staff involved in operations in Greece during the period. Draft summary information sheets were prepared for each project and preliminary findings were incorporated in two separate desk studies, one for projects in the transport sector and one for all other projects, to assist EV in determining the scope and depth of the next stage.

The second stage involved visits to project sites in Greece and detailed discussions with project promoters for an in-depth evaluation of a representative sample of projects in the EIB’s portfolio. In all, nine individual projects⁴ and two global loans (of which five sub-projects were visited) were evaluated. The evaluation covered four different types of projects in the electricity sector⁵ and one project each in highways, urban transport, telecommunications, mining and water supply and sewerage sectors. The sub-projects included four in the tourism sector, financed through one financial intermediary, and one in electric power generation from a wind energy source financed through another intermediary. Evaluation reports were prepared for each project and sub-project, using ECG criteria and incorporating new or revised information sheets as appropriate.

⁴ Three more projects (two road projects and an airport project) were initially planned for field visits; however, they could not be arranged within the timeframe of this evaluation.

⁵ These were a lignite-fired thermal power plant, an oil-fired combined-cycle thermal power plant, a run-of-river hydroelectric plant and a project to reduce polluting emissions of two thermal power plants.

2 Greece and EU Regional Development

2.1 Contribution of the EC and the EIB to Convergence

The EIB is significantly more active in Greece than in most other European regions: the Bank, on average, has financed 1.7% of the Gross Fixed Capital Formation (GFCF) of the EU15 between 1996 and 2000 compared to 4.4% of Greece's GFCF. The Bank's contribution to investment in the country is therefore more than 2.5 times higher than average in the EU, and it is the second highest ratio (after Portugal) among the Cohesion countries⁶.

Under the first two Community Support Framework (CSF) programmes for Greece (1989–93 and 1994–99) it was foreseen that the EIB would provide loan disbursements of EUR 1,307 m (1989 prices) and EUR 2,368 m (1994 prices) respectively. These would mainly contribute to the public sector's share of the overall CSF programmes of EUR 14.3 billion (1989 prices) and EUR 14.0 billion (1994 prices) respectively. For both programmes, the European Commission (EC) was expected to contribute about 50% in grants. Actual EIB disbursements (in constant prices) were higher than forecast, at EUR 1,496 m for 1989–93 and EUR 4,389 m for 1994–99.

Under CSF 1, the main priorities for joint actions by the government and the EC at the national level were:

- Upgrading the country's basic infrastructure;
- Development of the primary sector and rural areas;
- Improvement in the competitiveness of firms;
- Balanced development of tourism; and
- Development of human resources.

Under CSF 2, the main priorities were:

- Reduction of the degree of peripherality and promotion of integration by the development of large infrastructures;
- Improvement of living conditions;
- Development and competitiveness of the economy;
- Development of human resources and promotion of employment; and
- Reduction of regional disparities and opening up of island areas.

The EC and academic institutions have undertaken a number of recent studies on the effectiveness of the two CSF programmes⁷. The general conclusion is that the impact

⁶ The ratios of EIB lending/GFCF over the period 1996–2000 are: Portugal 5.7%, Spain 2.7% and Ireland 1.3%.

⁷ Bougas, T., "The Evaluation of Structural Policies", *Topos*, 7 (1994): 105–20 (in Greek). Christodoulakis, N., and Kalyvitis, S., "The Effects of the Second Community Support Framework 1994–99 on the Greek Economy", *Journal of Policy Modeling*, 22 (2000): 611–24. Economou, D., "The Impact of the First Community Support Framework for Greece: the Anatomy of Failure", *European Urban and Regional Studies*, 4 (1997): 71–84.

on annual GDP growth was just 0.3% in Greece, compared with 0.7% in Spain and Ireland and 1.0% in Portugal. For CSF 2 the conclusions are similar, but with the caveat that the impact on GDP in Greece is likely to be temporary.

2.2 The EIB's Project Portfolio in Greece, 1989-2000

The projects signed and fully or substantially completed⁸ during the period 1989-2000 were covered by the two desk studies⁹, including some for which loan tranches were signed before 1989. In all, 56 projects were reviewed in detail and a further 10 projects, relating to those completed but still under implementation, were reviewed in less detail.

The 56 projects comprised:

- 21 in the transport sector, including 10 inter-urban road projects, five urban transport projects, two railway projects, three air transport projects and one port project;
- 15 in the electricity sector, including four thermal power plants, two hydropower plants, three transmission and distribution projects, one lignite mining project, one island interconnection, one pollution reduction project and three loans for small-scale electricity projects¹⁰;
- Six in the telecommunications sector, including five for private mobile telephone companies and one for public fixed-line services;
- Three projects in other infrastructure sectors, including two in water supply and sewerage and one in natural gas supply;
- Four framework loans¹¹ for a variety of small projects, including two in infrastructure and one each in environment protection and information technology; and
- Seven global loans using seven different financial intermediaries for on-lending funds to small and medium size enterprises (SMEs).

The 10 projects still under implementation comprised six global loans to four different financial intermediaries, three electric power projects (two thermal plants and one for transmission and distribution) and one natural gas supply project¹².

⁸ I.e. in operation or cancelled. In a limited number of cases, the evaluation also included projects that should have been completed but were not, due to substantial delays in project implementation.

⁹ Four direct loan projects, all identified in 1987 with contracts signed in 1988, were not included in the review although they had a tranche signed in 1989. Two were small irrigation projects which faced such considerable problems that the Bank decided not to finance similar projects later on in the decade. One was an earthquake rehabilitation project which was a special (and not very successful) case and one was a technical training centre which is not representative of the more recent education projects carried out by the Bank in Greece. The more recent education projects had not been completed at the time of the evaluation and hence not included in the review.

¹⁰ Two of these loans are framework loans.

¹¹ Framework loans and global loans are both intermediated but global loans are usually to financial intermediaries while framework loans are to other companies (e.g. electricity companies) or public institutions. The financial intermediary of a global loan shares the credit risk with the Bank, which is not the case for framework loans.

¹² Essentially the same as the one mentioned above, for which the Bank cancelled the loan before contracting a new one for the same project, eight years later with a new project appraisal, having continuously followed up the project in the meantime.

All the projects in the portfolio are broadly consistent with recent EU objectives, either in terms of regional development or of specific sectors. Yet, as will be shown later, the portfolio has not been based on an active portfolio management strategy designed to maximize the Bank's contribution to promoting convergence. Neither has it contributed significantly to the priorities and objectives of the CSFs for Greece, except in the areas of upgrading basic infrastructure (CSF1) and promoting regional integration by large infrastructure projects (CSF2).

For the 56 projects evaluated, the Bank's contribution in EUR million was as follows:¹³

	PLANNED	% PLANNED	ACTUAL	% ACTUAL	% Actual/ Planned
Transport	4,555	70%	3,855	71%	85%
Energy	691	11%	676	12%	98%
Water & Gas	315	5%	67	1%	21%
Global Loans	101	2%	73	1%	72%
Framework Loans	291	4%	216	4%	74%
Telecommunications	529	8%	528	10%	100%
Total	6,482	100%	5,415	100%	84%

With the exception of one large loan in the gas sector that was cancelled (although the project benefited from a new loan later on) and two global loans that were basically not used, there has been a satisfactory level of disbursement (84%) on signed contracts. However, if the three largest transport loans (disbursed at 91% of the expected amounts) are excluded, the actual disbursement in the transport sector has been only 74% of the planned lending, which reflects the difficulties faced by a number of the projects.

Out of the 56 projects, only 11 were purely private sector projects. Thirty-nine projects were purely public sector projects and represented 57% of the disbursements. Six were a combination of private and public shareholding, mainly large projects representing 37% of the total amounts disbursed by the EIB in Greece over the period¹⁴.

The size of the loans has varied greatly. Three individual loans in the transport sector were each larger than the 15 loans to the electricity sector and represented together 44% of planned amounts and 48% of disbursed amounts of the 56 loans.

The Bank's lending activities in Greece have significantly increased in the latter part of the decade. The Bank is investing in new sectors such as health and education (7% in 1996-2001) and transport now represents more than half the signed amounts, whereas lending to the industry sector only represents 2% of the contracted amounts. The portfolio of the 190 contracts signed covering 103 projects between 1989-2001 (including those still under completion) is as follows:

¹³ Slight variations in figures may be given by different information sources of the Bank's data warehouse.

¹⁴ This would appear to result, in part, from the fact that many public sector or combined public-private projects benefited from government guarantees that made EIB financing more attractive.

Contracts signed between 1989 and 2001

	Amount in EUR of contracts signed 1989-1995	Amount in EUR of contracts signed 1996-2001	Share of total for the period 1989-1995	Share of total for the period 1996-2001
Transport	986	4,211	36%	60%
Electricity and mine	453	658	16%	9%
Industry	4	150	0%	2%
Water & gas	78	300	3%	4%
Earthquake reconstruction	72	550	3%	8%
Telecommunications	340	189	12%	3%
Health and education (new EIB activity)	11	500	0%	7%
Global loans	302	228	11%	3%
Framework loans	501	290	18%	4%
Total	2,746	7,076	100%	100%

Financial intermediation, tourism and manufacturing represent respectively 4.7%, 6.6% and 13.0% (amounting to 24.3%) of total value added in 1998; in contrast, the contribution of the Bank to these sectors (through global loans) only accounts for 6% of its lending in Greece over the last ten years. Similarly, almost 4% of the Greek labour force is employed in high tech industries, but there are no EIB loans in that sector. In addition, the Bank has not contributed significantly by direct lending to the fast-growing sectors, although, arguably, its contribution to basic infrastructure had an impact on other sectors as well.

So although the period under evaluation was characterised by a high increase in lending volume, the Bank does not appear to have exhausted its investment opportunities.

3 The Performance of the EIB's Operations in Greece

3.1 Project Identification, Selection and Relevance

The evaluation of the 56 projects found that there was no discernible pattern relating to regional development objectives in the identification and selection of these projects. With the notable exception of projects in the electricity and telecommunications sectors, discussed below, there appears to have been no formalised or structured project identification process and certainly no pro-active approach to identifying and prioritising projects aimed at promoting convergence. The Bank has established particularly close contacts with the Greek authorities and most of the projects seem to come through this channel. The promoters themselves present most other projects to the Bank. The identification process is therefore essentially reactive. It should be noted that the period under review predates the implementation of medium term planning through a corporate operational plan (COP), the first of which was produced in 1999, which has the potential (yet unrealised for regional development) for establishing specific lending strategies for individual countries.

Nevertheless, there have been several (sometimes undesirable) common features in project identification and selection. One is that the EIB has been asked to finance projects, particularly those in transport and the other infrastructure sectors, at a relatively late stage in the project cycle¹⁵. This effectively means a 'take it or leave it' decision for the Bank. A brief review of projects rejected during the period (carried out as part of the evaluation) concludes that the decision has usually been to 'take it'. In one case, the project loan was hurriedly processed and signed less than one month before project completion¹⁶, even though the Bank's economists calculated that it had a negative ERR. The Bank agreed to finance projects that were over-dimensioned or over-designed. This was the case for at least seven of the ten highway projects evaluated.

Discussions between the evaluators and the services have highlighted three constraints that prevent the Bank from turning down projects lacking sufficient regional development justification. First, turning down a project could imply that annual lending objectives per country might not be achieved. Second, there is the understanding that the Bank has a form of "public service obligation" and as such it feels compelled to contribute to prominent projects even when poorly designed or with a weak institutional set-up, as long as there is no prospect of correcting the design or the institutional framework within the timescale of the project. Third, EIB staff have an understandable reluctance to contradict the European Commission and will tend to adopt a more lenient attitude towards projects that have already received (e.g. through the allocation of grants) the support of the EC. Although it should be noted that some staff members maintain that past project failures were not repeated

¹⁵ Staff have pointed out, however, that they often get involved much earlier than it would be apparent from the formal appraisal process. In particular, projects that are rejected very early on in the process are not documented.

¹⁶ Under its regulations, the Bank cannot finance completed projects.

because of a learning process which has helped improve the management of more recent projects.

In the few cases when the EIB has rejected proposed projects, it has been for one of three main reasons. The prime reason has been ‘self-rejection’, with the promoter failing to follow up his initial request for finance. In some cases, this was because the promoter had found finance elsewhere; in others, particularly in the public sector, the promoter or the Bank (sometimes as a way of dissuading a bad project) did not maintain communications. The second most important reason for rejection has been the poor past performance of the promoter in implementing previous EIB financed projects. A third (entirely appropriate) reason has been that the proposed projects raised serious environmental concerns.

A second common feature about project identification and selection is that the Bank has accepted the available project documentation, which, in some cases, was inadequate or incomplete. In general, the Bank’s staff have been reluctant to press the project promoters for further information. This could be to maintain the scheduled lending programme or because previous attempts to obtain more information from the same promoters had proved unsuccessful.

The projects selected without appropriate technical, economic and financial justification or environmental assessment later faced implementation delays, cost escalation, contractual disputes, and sometimes were abandoned¹⁷. In some cases, deficiencies of documentation were reflected in disbursement conditions for the loans or later tranches of these loans, but those conditions were not always enforced. In a number of cases, the problem stems from the fact that official undertakings accepted by the Bank (e.g. relating to irrigation or to pollutant emissions) were either ignored or carried out with substantial delays. However, in most of these cases, the appraisals carried out by the Bank also underestimated the impact of institutional issues.

For four large framework loans, which were essentially presented to the EIB rather than selected by the Bank, there was practically no technical or other information available concerning the many small schemes to be financed. According to the reports on allocations, a considerable number were never carried out.

A third common feature has been the apparent willingness of the EIB to follow rather than lead or participate in the selection process for the projects that have also received grant funding from the European Union’s cohesion, structural or other funds. Over 30 of the 44 projects that were not global loans or loans to private (mobile telephone) companies received such funding. Fifteen of these 30 projects were in the transport sector. While this is consistent with policies on cooperation between the EIB and the EC under the CSFs, in most of these cases it seems the selection was essentially carried out by the EC, with hardly any impact of the Bank in the process.

¹⁷ In the evaluators’ opinion, this led to an insufficient quality of appraisals in nearly half the cases. Of the 56 projects evaluated and financed by the Bank in Greece over the period 1989-2000, 7 should never have been selected and 19 projects, of which 11 were in the transport sector, should not have been appraised by the Bank based on the design and documentation available. See section 3.8.

In many projects, including some of the problem cases, the ways in which project selection and appraisal were carried out was influenced by the fact that most of the projects were presented by the Greek government, i.e. one of the Bank's shareholders, with a loan guarantee by the Hellenic Republic.

In the past, steadily increasing annual lending targets were set on a country-by-country basis. Helping a promoter with a difficult project was seen as an important aspect of a continuing relationship, especially in the public sector. In addition, then and now, the appraisal process usually takes up a considerable amount of limited staff resources. As a result, turning down a project at appraisal is seen as a disruptive event. This explains why even appraisals with a negative conclusion were presented to the Management Committee for approval and normally passed on to the Board of Directors. This also explains why 17 of the 56 appraisals contained overoptimistic conclusions about the projects or their promoters.

The drafting of appraisal conclusions and their subsequent inclusion in the Board report is overly complex with numerous formal (and even more informal) opportunities for redrafting. Simplifying the process would result in productivity improvements, leaving staff with more time for more systematic project identification. It would also result in more accurate reporting. Redundant redrafting steps tend to result in bad news being softened or edited away (to such an extent that the Board may not always have been in a position to realise that the technical and economic services had delivered a negative opinion on some projects).

Weak for infrastructure and global loan projects, the identification and selection processes for the EIB's projects have been more effective in the electricity and telecommunications sectors in Greece. During the period under review, the EIB has regularly assessed the performance and prospects of the main promoter by undertaking electricity sector studies in 1989, 1992, 1993, 1994 and 1999. These studies covered all aspects of the promoter's operations, including demand forecasts, investment programmes and management capabilities. The EIB's engineers have met regularly with the promoter for project identification, preparation and monitoring. For its part, the promoter has provided the Bank with regularly updated information on its investment programme and regular progress reports on all major projects. As a result, the selection of projects has had both rationality and relevance, even if (as noted below) it concentrated on thermal power generation and transmission projects. Of particular importance in this respect was the promoter's clear understanding of what underlying technical, financial, economic and other information the Bank required for each proposed project. The promoter has also been mindful of various aspects of the EU's common energy policy, such as the promotion of indigenous fuels or substitution of polluting fuels by less-polluting fuels. A particularly noteworthy aspect of the Bank's lending to the sector has been its successful use in six cases of what were essentially framework loans covering an investment programme of small-scale projects¹⁸.

¹⁸ This 'programme approach' is now a recognised policy of the Bank, with guidelines for justification and criteria related to both the project and the promoter.

In telecommunications, one of the six loans made (for fixed-line services) was based on the recommendations of a detailed sector analysis carried out by independent consultants jointly financed by the EIB and the EC in 1991. The other five, to mobile telephone companies with experienced foreign (other European) partners, were based on the regular and detailed studies carried out by the EU as part of its review of the implementation of the Telecommunications Regulatory Package¹⁹.

3.2 The EIB's Impact on Project Costs, Financing and Procurement

For Greece, during the period under review, the advantages of borrowing from the EIB have been substantial. Compared with the cost to the Greek Government of borrowing from commercial sources, the Bank's loans were more advantageous both in terms of the cost of capital (by an estimated 100 basis points) and in terms of longer maturity (up to 25 years). Indeed, in the early years of the period it would probably have been impossible for the Government to obtain commercial loans with anywhere near such maturities and interest rates. In addition, the global loans made to financial intermediaries for on-lending to small and medium sized enterprises (SMEs) in the private sector provided medium term finance that was unavailable from other sources.

The Bank's loans have had three important beneficial effects on the national budget. First, the Bank's cost of raising capital is low because of its triple A rating in the money markets and therefore its on-lending terms have been favourable compared with other sources of financing, including the issuance of bonds by the Greek state²⁰. Second, the fact that a triple A rated EU institution supports projects in Greece has provided 'comfort' to commercial lenders and the private sector. This 'goodwill' has been very important in encouraging the private sector's financial participation in several major infrastructure projects, thus reducing the Government's debt burden. Third, the substantial resources provided by the Bank have enhanced the Government's own borrowing power. The EIB's contracts signed with the public sector and mixed public/private institutions with public service objectives reached six billion EUR over the period under review.

In all the evaluated projects, the EIB's loans have played a significant role in the financing. The Bank can normally finance up to 50% of the total estimated costs of

¹⁹ However, all appraisal reports carried out between 1993 and 1997 ignored (for the older reports) or severely underestimated (for the more recent) the threat of entry by the fixed operator (who entered the market in 1998 and had a 35% market share by 2000). This illustrates the difficulty of making accurate forecasts in a new and fast-expanding market; it may also indicate the need for the Bank to strengthen the analysis of competition in its appraisal reports.

²⁰ For example, in the early 1990s the yield spread between 10-year DM bonds issued by the Greek State and those issued by the Bank was around 150 basis points. However, by the year 2000 the spread between Greek bonds and Bank bonds has narrowed significantly because of conversion speculation concerning the country's membership in the euro monetary zone. The average yield spread for a 10-year bond at the beginning of 2000 was about 39 basis points.

projects²¹. Of the 44 individual public sector projects, 27 indeed received finance of around 50%. These included 11 of the 15 projects in the electricity sector and 13 of the 21 projects in the transport sector.

In several instances the Bank's loan actually financed more than 50% of the total cost as estimated by the project promoters. This was because the EIB legitimately includes 'contingencies' and 'interest during construction' in its estimation of the total cost of the projects before applying the 50%. However, this convention does not appear to be followed in the same way by most of the Bank's borrowers. Many of the project promoters interviewed during the evaluation, while recognizing the need to include 'interest during construction' as a legitimate cost, did not consider the 'contingencies' to represent reality and did not incorporate them in their costing or financial reporting of the projects. In the absence of precise guidelines, it is difficult to distinguish increases in contingencies that address a particular risk from those that boost the project cost, and hence the maximum loan amount, artificially.

For 11 projects in the transport sector VAT was also included in estimated total costs, again resulting in the Bank financing a substantially greater percentage of the real total costs than was indicated by the figures presented in the appraisal reports. New guidelines issued in 2001 by the technical and economic services should avoid this in future if they are strictly adhered to.

The evaluation of projects in the electricity sector presents a somewhat different picture of the EIB's financial contribution. During the period 1989–2000, the Bank contributed a very limited share to the main promoter's overall investment programme. The Bank's main emphasis was on financing thermal power stations on the Greek mainland, together with associated lignite mines, and transmission lines. In no other area of investment in the sector, including hydropower plants, island thermal stations, renewable energy or electricity distribution, did the Bank's contribution reach a significant level. This raises the question (also raised by the promoter during the evaluation) whether the EIB could have provided much more investment finance to the electricity sector, thus reducing the costs of the promoter's external borrowing, particularly since, as noted in the previous section, the Bank's project selection process was of a particularly high standard in this area.

The EIB also lent directly to private telephone companies that had major partners from other European countries and had obtained licenses in 1993 to introduce and spread mobile telecommunications in the country. These companies could draw extensively on their own financial resources and the Bank's loans were only needed to assist in the initial stages of investment.

The EIB's loans in conjunction with EU grants are not supposed to amount to more than 90% of the total project costs²². For more than half the loans to the transport sector this percentage was approached or reached, with the contribution from the national budget accounting for only 10–15%. Many of the large EU grants to the transport sector were earmarked for financing a set percentage of the cost of specific

²¹ See Decision of the Board of Governors, June 4, 1984, section 1.6. For a project that goes well beyond EU environmental standards it can finance up to 60% and for Edinburgh Facility loans (a temporary measure) it could finance up to 75%.

²² EU, 'L'Europe au service du développement régional', 1996, p.5.

projects (e.g. TENs). This created an incentive to over-design such projects. Despite this, there is little doubt that without the financial participation of the EIB and the EU the modernization of the Greek transport sector during the 1990s would have been much slower than it was.

The four large framework loans all received grants from the EU to bring the EIB/EU contribution to 90%. Each loan was to finance a large number of small-scale and highly dispersed infrastructure schemes, and therefore difficult to keep track of. As the actual total costs of the four projects turned out to be considerably lower than forecast, largely because many of the sub-projects were not implemented, it is likely that the contribution from the national budget was less than 10%.

For two infrastructure projects, serious concerns were raised in the appraisal reports about the ability of the promoters to finance the gap that remained after the EIB/EU contributions and the promoters' own resources. In one case funds had to be obtained from the national budget; in the other they were to be obtained through unspecified medium and long term loans from abroad. In both cases, these concerns proved to be well founded. In the first case, project implementation faced serious delays; in the second, the project and its financing had to be renegotiated with the EIB after a stalemate lasting several years.

It is noteworthy that in only a handful of the appraisal reports for the evaluated projects there was any serious analysis of cost-efficiency. In addition, it is understood that there were rarely, if ever, detailed discussions with the project promoter about ways to increase cost-efficiency, or at least these are not reflected in the appraisal reports. In several reports for electricity projects, total costs were simply considered to be 'acceptable for the type of project' (sometimes 'high but acceptable') or 'similar to those elsewhere in Europe for similar schemes'. For several transport projects that were over-dimensioned, this fact was noted but the projects were approved anyway. There seems to be a lack of clear guidelines (and lack of agreement among staff in different sectors) on how to ensure that projects are not over-designed. The principle enforced in other International Financial Institutions, that all oversized projects should be rejected unless they can be redesigned and downsized, does not seem to be universally accepted in the Bank, even by its economic and technical services.

An important contribution to the cost-efficiency of a project is the way in which the various goods and services needed for implementation are procured. The transport sector procurement procedures, with one exception, have generally been in accordance with the relevant EU Directives.

For other sectors and types of loans, the EIB had a marginal impact on the procurement procedure. For the period under evaluation, EU Directives were not officially applicable in Greece outside the transport sector. The Bank's technical staff therefore assessed whether the procedures were appropriate or acceptable on a case-by-case basis²³. For only one of the 28 individual projects outside the transport sector was international competitive bidding (ICB) used; less stringent procedures were used

²³ The engineer in charge of the project appraisal usually documents this assessment outside the appraisal report, in notes and correspondence with the promoter and, in case of difficulties, notes to file or notes to the operational directorate.

in all other cases²⁴. In at least one case, the guidelines appear to have been loosely interpreted: the appraisal report mentions that the procurement procedure was accepted, although it was stated that it would normally not be.

Gradually, the public sector companies are complying with the relevant EU Directives and matching the efficiency of their EU counterparts. The ‘crash programme’ of a public sector telephone company, carried out partly on the instigation of the Bank, dramatically improved the quality and availability of fixed-line services, transformed analog systems to digital and established the foundation for company to move into other modern telecommunications activities in both Greece and neighbouring countries. In electricity, the Bank staff also claim some influence on the company’s evolution (for instance, the streamlining of administrative staff was recommended by the Bank and subsequently carried out), although this could not be proved during the evaluation.

3.3 Impact on Project Implementation and Performance

Of the 56 projects reviewed by the evaluation team, 2 global loans, 2 framework loans, 4 transport projects, 1 water project and 1 gas project failed substantially to achieve their overall physical objectives.

Even when physical objectives were met, implementation was not always timely or smooth. 29 projects faced substantial delays in implementation for a variety of reasons, including contractual disputes, design problems or changes, land ownership disputes, natural disasters (such as floods), geological or archaeological surprises, the requirement to complete an environmental impact assessment (EIA) or poor coordination between different ministries and/or local authorities. In 22 of these cases, there were significant cost overruns.

However, not all delays were due to project management weaknesses; some, particularly for some public companies in the early 1990s, seem to have been the consequence of protracted budgetary negotiations at the national level. In some sectors, especially water supply and transport, regular experience of project delays did not lead to promoters extending their project implementation schedules. In a number of cases, particularly in the transport sector, the Bank’s engineers factored such delays into their appraisals but these were often still short of reality²⁵.

The telecommunications sector was the only one to avoid implementation problems. All six projects emerged as extremely successful investments, meeting all their objectives, being completed on or ahead of schedule and with only marginal differences between forecasted and actual total costs.

²⁴ Actual procurement procedures in the remaining 27 projects depended largely on the project promoter and included direct allocation to a Greek firm, direct allocation to a Greek/international consortium, national enquiries, national tendering, international enquiries and international tendering.

²⁵ Underestimating delays normally results in overestimating the rate of return of the project.

There has been considerable evolution in the way public sector projects have been implemented. At the beginning of the period under evaluation, government ministries assumed direct responsibility for implementing clusters of projects, often without adequate project design and project management expertise. One of the main contributory causes of contractors' poor performance was the delay in payments by the administration. This compromised the contractors' performance in some cases; in others, it led to stopping the work. There also appears to have been poor communication (including physical and financial monitoring) at the time between the government ministries and the local authorities that were, in many cases, the beneficiaries. In more recent times, particularly for large transport projects, single-purpose entities and decentralised agencies, with the involvement of private sector partners, are carrying out projects on an individual basis in what is expected to lead to more efficient operations.

The Bank's monitoring of project implementation has been based on regular progress reports from the promoter with the main emphasis being on physical implementation and financial disbursements²⁶. In the electricity and telecommunications sectors, these reports were timely and complete; in other sectors, some were late and incomplete. In the electricity and transport sectors, the reports were channelled through the Bank's Athens office, whose staff added its own comments or covering report, to headquarters where decisions were taken on follow-up measures. Depending on the extent of any problems identified, these measures took the form of further visits by the EIB's Athens staff, visits by the Bank's project engineer or, in the most extreme cases, hiring of a technical consultant to assist the project promoter. The Bank should establish objectively verifiable indicators to detect problem projects and to implement appropriate corrective actions.

In effect, the Bank appears to have paid insufficient attention to the importance of adequate and timely implementation and monitoring of project profitability and sustainability. Delays in project implementation usually have a negative effect on profitability. In one road project evaluated, for example, delays reduced the benefits calculated in the appraisal report by up to 80%.

For global loans, there is no monitoring apart from checking the eligibility of allocations. The selection of sub-loans is a passive process, whereby the financial intermediary proposes sub-loans for specific projects to the Bank for review. Where global loans failed to deliver, the Bank simply did not disburse the loan to the intermediary. However, no efforts seem to have been made to assess the reasons for the problems. More generally, the credit risk analysis or project supervision capabilities of the intermediary, once appraised, were either not monitored, or only indirectly through a new loan appraisal if one was in preparation.

Monitoring of some framework loans has not proved particularly effective either. A complicated series of central and regional monitoring committees, project monitoring teams, programme managers and computerised monitoring systems were established.

²⁶ Monitoring has not extended to checking actual against forecast demand for the project's output, dealing with employment or skills issues, reviewing management or organisational problems, evaluating technical changes in the scope of the project, assessing facilities for repair and maintenance, following up problems predicted in the appraisal report or recommending measures to ensure the future sustainability of the project.

The programme managers regularly submitted diskettes to the EIB with the results of the monitoring. These were only occasionally checked for reliability during field visits by the Bank's staff. The findings for one sample of 11 diskettes are probably representative. They showed that in five cases the monitoring was unsatisfactory and in a further four the information was incomplete. As far as can be determined the EIB did not attempt to remedy this situation.

Although the Bank has no formal mechanism for dealing with problem projects, the experience with five major transport or other infrastructure projects that faced severe difficulties during the period suggests two courses of action that can be both beneficial and effective. One (adopted for three projects) is to suspend disbursements and re-appraise the project, making a new loan if the revised project can be made profitable and sustainable. The second (adopted for the other two projects) is to provide the promoter with technical and/or managerial specialists to improve project performance. The EIB appears to have been reluctant to cancel failed or failing projects, unless requested to do so by the promoter, though in several instances this could have been a less costly course of action for the Bank, which had to devote a disproportionate amount of resources to deal with these problem projects.

However, staff involved have argued that the presence of the Bank in these few exceptional cases was important and beneficial: through these projects, the Bank contributed to long-term institutional development. For instance, the Bank contributed confidentially but substantially to the resolution of a number of contract disputes. It requested (and helped finance) the development of a 20-year business plan for a large urban transport project that soon became a reference and benefited all the transport organisations in Athens. It provided discreet support to the Government towards the adoption of a number of technical regulations when it became apparent through project reviews that such elements of the institutional framework were missing. In addition, the Bank has acquired considerable experience in the legal structure and negotiation of complex projects, involving for instance public/private partnership, and expects to be able to make good use of this experience in future.

More generally, staff have pointed out the very difficult institutional and business environment in which many of the projects have been identified, appraised and implemented/monitored. They pointed out that, over the period under evaluation and especially at the start, many EIB counterparts in Greece had difficulties performing their role for political, resource, personnel or other reasons, which made timely and accurate project completion difficult.

3.4 Project Profitability and Sustainability

3.4.1 Ex-ante Profitability Calculation

The ERR is the most commonly promoted measure of a project's potential profitability, with the financial internal rate of return (IRR) being a useful proxy in revenue earning projects. However, for 23 of the 56 projects evaluated in Greece, neither the ERR nor the IRR could be realistically calculated at the time of appraisal (or ex-post). This raises serious questions about the relevance and value of the ERR as a single, all-encompassing project selection indicator.

For the seven global loans, as is normal for global loans, no information was available about the sub-loans that were expected to be made. For the four framework loans, there was insufficient information available about the sub-projects to be included. For four of the 15 electricity projects an ERR was calculated, because these were the ones in which the investment and returns could be ‘isolated’ from the overall activities of the promoter. For nine other electricity projects, the levelised cost²⁷ was calculated. In six projects, this was done by calculating the discounted incremental average power cost (assuming the life of the project (always 15 years) and a discount rate (always five percent)). In three others, it was done by comparing the investment costs with costs of similar projects elsewhere in the EU. The impossibility to isolate the investment also applied to the project for fixed-line telecommunications.

As will be shown below, for the 21 transport projects, the ERRs (or ‘first year rates of return’) calculated were methodologically unsound or inconsistent. Of the other eight projects, five were to private sector mobile telephone companies, for which there was no difficulty in calculating the (high) IRR or return on assets, and three were stand-alone infrastructure projects.

In the transport sector, the ERRs of the projects were difficult to compare because, for the period under evaluation, there was no methodological consistency in their calculation. A detailed analysis of the components of the benefits underlying the ERR calculations identified the following deficiencies:

- Although timesavings accounted for 60 to 90% of estimated project benefits, no common scientific and methodological basis was used for their valuation in the Greek context or for their development over time. Each appraisal team appears to have adopted its own assumptions. Furthermore, there is now some evidence²⁸ to suggest that many of the project appraisals over-estimated the value of time by about 30%. Estimates of growth of the value of time are similarly disparate, ranging from 0% to 2.5%.
- The reduction of road accidents was another quantified benefit, accounting for about 10% of the total benefits. Again, there was no consistent methodology in the calculations, which were generally assumed to be 3–4 Greek drachma per vehicle/kilometre, nor any justification for assuming that the cost per accident would not increase with higher speeds.
- The new traffic generated by the projects, although a relatively insignificant part of total benefits, was consistently estimated at 10–15% of total traffic volume, but without any justification.
- There was no consistency in whether the benefits were calculated by adopting a ‘before – after’ project comparison or a ‘with – without’ comparison²⁹.
- In only two cases was an incremental investment analysis used to determine whether a project was over-dimensioned or would not provide sufficient capacity.

²⁷ Net present value of costs divided by net present value of output.

²⁸ See, for instance: Ioannis Spanos, Alexandros Deloukas, Anna Anastassaki, (1996) *A Stated Choice Experiment: Value of Travel Characteristics in the Context of Attika*, Athens University of Economics and Business.

²⁹ Some road project appraisals used the “before - after” project comparison. Project staff justified the practice as an attempt to stay on the conservative side of benefit estimation because it was seen as unlikely that the existing roads would be allowed to deteriorate beyond a reasonable threshold. An alternative way (and from a methodological point of view preferable) of accounting for such a maintenance policy was adopted in a number of other project appraisals, which took this scenario explicitly into account.

A review of the value of time for EU countries was prepared in 1994 by the technical and economic services of the Bank, but appears not to have been used in the practical work of the Bank. The recent adoption of new software for establishing the parameters of the economic justification of transport projects should provide the technical possibility to address most of these problems in the future.

The extent to which these inconsistencies are addressed very much depends on the objectives that the project appraisal team assigns to the appraisal. Some Project Directorate staff have pointed out that they see the primary objective of appraisal as simply determining whether the project is acceptable for financing. This modulated procedure results in focusing on the economic benefits only to the extent necessary to yield an acceptable rate of return. In other words, the calculation will be more sophisticated for marginal projects and only broad-brush for the more profitable projects. This means, however, that the ERRs calculated are not comparable with one another and tend to underestimate the benefits of the better projects, i.e. those where the regional development impact is likely to be more demonstrable. In addition, the parameters selected on an *ad hoc* basis are often the result of limited analysis only.

Estimation of the ERR or levelised costs in the electricity projects showed more consistency and rationality. Nevertheless, whatever the results, they were in all cases ‘acceptable’ for the Bank without further justification, without discussion of the relevance of the assumptions and without consideration of how the projects would promote convergence.

More importantly, estimation of the ERR of a project appears to have had little or no impact on whether a project was considered acceptable and therefore approved. Five of the approved projects for which an ERR had been estimated had a negative or only marginally positive ERR (under five percent). Some (separable) components of transport projects had very low ERRs even though the overall ERRs of the projects were at acceptable levels. No attempts were made in the appraisals to eliminate or redesign these components.

3.4.2 Ex-post Assessment

In the transport sector, the ex-ante rates of return do not provide a good starting basis for an ex-post assessment for the reasons explained. But if there is a 30% overestimate of value of time in some appraisals, the delays of more than a year for nine of the projects and cost-overruns of more than 10% for eight of the projects, profitability ex-post must in general inevitably be less than ex-ante profitability. In 11 cases, the transport projects are not economically sustainable (negative return ex-post or no long-term sustainable solution). These conclusions are based on the ex-ante demand levels (and ex-post cost levels), as the ex-post traffic figures were simply not available.

In the mobile telephony sector, demand is now a third higher than forecast by the Bank at the time of appraisal and the average revenue per user (ARPU) is slightly below, but close to, what the Bank forecast. As the ex-post costs are in line (within 5%) with original estimates, the profitability of mobile telephony in Greece is higher than expected. This does not mean, however, that the profitability of individual

projects is higher than expected by the Bank ex-ante, as several appraisals did not foresee the successful entry of a third operator into the mobile telephony business and did not include this parameter in the forecasts.

In the energy sector, one large project now has a rate of return close to zero. The profitability of the mining project cannot be further assessed in the absence of detailed cost data but the mine production, both in terms of weight and calorific value, has been higher than forecast. For the three power plants evaluated in detail, the ex-post unit cost turned out to be higher than expected, due to cost increases in one case and to project delays in another. In the third case, the plant proved, as expected at appraisal, to have a cost that would be high and only acceptable for a small island.

For the water project evaluated in detail, the water supply component failed to reach its objectives while the water treatment one was fully satisfactory. The cost of the project was below expectations.

Overall, 12 of the 13 electricity projects and all five telecommunications projects proved technically, economically and financially sustainable³⁰, i.e. such that they will continue to produce a positive technical, economic and financial impact in the long term future. Of the 21 transport projects, 17 were evaluated as technically sustainable³¹ and only nine as economically sustainable, of which one could face financial difficulties in the near future. None of the three (gas and water) infrastructure projects can be considered sustainable on every count. Of the global loans and framework loans, five turned out not to be technically sustainable (through lack of experience of the promoter).

3.5 Impact on SME Development through Global Loans

Seven global loans were reviewed in detail. These involved loans by the EIB to seven different financial intermediaries to on-lend funds to SMEs in the private sector. The main target sectors were industry, tourism and associated services, but projects for environmental protection and energy saving were also eligible. One of the financial intermediaries was the National Investment Bank for Industrial Development (ETEBA); the other six were private commercial banks. A further six global loans, still under implementation at the end of 1999, were also reviewed, but only briefly as the relevant reports on allocations had not been prepared at the time of the evaluation.

Processing of these loans within the Bank was extremely rapid, with all loans signed within weeks of project appraisal. Since the sub-loans would be to the private sector, EC Directives on procurement did not apply. All the intermediaries were given the EIB's requirements for sub-projects:

- Only those with fixed asset costs of less than 10 m ECU;
- Only promoters with less than 75 m ECU of fixed assets in total;
- A maximum for each allocation of 2 m ECU;

³⁰ Environmental sustainability will be discussed in a separate section, below. In the evaluators' opinion, all projects were environmentally sustainable.

³¹ With a design that sometimes differed substantially from the one presented to the Bank at the time of appraisal.

- No allocation more than 50% of fixed asset costs;
- No allocation less than 20,000 ECU;
- Priority to be given to SMEs (not more than 500 in workforce); and
- Priority to be given to new technology, innovation and energy saving.

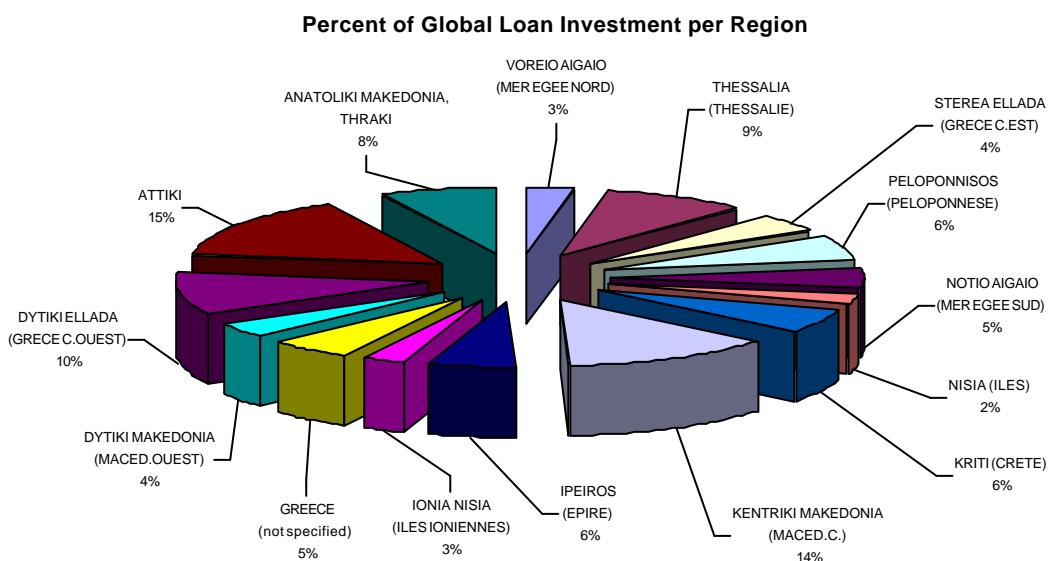
The EC's list of sectoral exclusions, primarily due to structural problems of overcapacity in the Community, was also provided. This had three categories:

- Sensitive sectors (mainly textiles and agro-industry): preference should be given to modernization or conversion over increases in productive capacity;
- Highly sensitive sectors (mainly agriculture): exclusion of increases in productive capacity; and
- Excluded sectors.

All seven intermediaries faced difficulties during the period 1990-91 because of the macroeconomic situation and high local interest rates (over 25%). However, five of the global loans were relatively successful, in that a reasonable number of sub-loans were made, although not as many as initially forecast. One global loan failed to make any allocation at all during the contractual period and the remaining global loan made only one allocation. For six out of the seven cases, take-up was slower than expected and extensions had to be granted to the contractual allocation periods.

Under the five reasonably good global loans about 70 allocations were made, with over 2,000 jobs created or secured. Most of the allocations were for tourism, for food and beverage, for electrical engineering and various forms of manufacturing. As for regional allocations, most were in Attiki and Central Greece, followed by Crete and the islands and then Central Macedonia, Thessaly and Thrace.

Considering all global loans signed between 1989 and 2000, there seems to have been a relatively even distribution of funds across regions:



Five projects, representing seven of the sub-loans made by two different financial intermediaries, were evaluated in depth through field visits. All the projects were very good, meeting all the criteria for relevance, efficacy, efficiency, impact and sustainability. For their part, the financial intermediaries showed that they had competent management and very satisfactory project appraisal, selection and supervision procedures.

Nevertheless, it was noteworthy that the promoters of all five projects were well-established businessmen with excellent credit ratings and that the projects were relatively large by normal SME standards. According to the senior management of one financial intermediary, this is common practice and is a major reason why there have been very few defaults on sub-loans. This raises the issue of whether there is a gap in the market for medium-term loans for smaller enterprises and less well-known project promoters. If so, it must be questioned whether enough global lending has been made to Greece and whether there has been sufficient competition among financial intermediaries in Greece for the EIB's resources, particularly since the country's economic situation has shown significant improvements in recent years.

3.6 Impact on Employment

This evaluation also set out to review what has been achieved by the Bank-financed projects in the area of employment creation but came across very significant obstacles in gathering meaningful data. Ex-ante, it is very difficult to double-check the claims made by the promoters regarding the number of jobs to be directly created during construction and during operations. Ex-post, these numbers often prove even more difficult to verify, in particular because many jobs are not earmarked with reference to a particular project but contribute to the overall operations of the promoter. As to the indirect employment effects, which can be very significant, in particular for infrastructure projects, these can only be assessed through a broader and very labour-intensive impact analysis³², which is beyond the scope of this evaluation.

Employment creation is one amongst a number of criteria in the selection, appraisal or processing of EIB projects. The appraisal reports have generally accepted the promoter's estimates of the number of temporary and permanent employees needed by the project, while the monitoring and completion reports have reported briefly the actual figures. For most projects, the numbers are extremely small compared to the national workforce of about four million. For example, the five global loans that were relatively successful are believed to have created or secured some 2,000 jobs. There were 2,000 new jobs created by the introduction and rapid development of the mobile telephone network and 2,040 new technical jobs under the 15 projects in the electricity sector, though at the same time the company was reducing its overall management, administration and unskilled staff at the instigation of the Bank.

³² This requires the estimation of the employment multiplier effects but at a level of detail where statistical information is rarely available. Therefore, the primary task of such analytical studies is often to complement existing statistical data through extensive surveys.

Investment in transport and other infrastructure projects has, however, had a somewhat more significant short-term impact on employment. For the 21 transport projects reviewed, short-term employment creation has been estimated at 132,000 person years with (gross) creation of permanent employment estimated at 7,100 persons, though how much of this was additional is difficult to determine without further study³³. However, it must be noted that inadequate transport in Greece has clearly been a limiting factor to the more efficient production of goods and services in other economic sectors, and adequate access is a pre-condition for other sectors to flourish and compete. Consequently, the direct employment effects of transport infrastructure should probably be accorded secondary importance to the role of transport in increasing the overall production efficiency of the economy and in promoting the allocation efficiency of all available resources, including labour.

Equally important have been the employment multiplier effects flowing from new or upgraded facilities and, particularly, higher productivity and efficiency in sectors such as electricity and telecommunications. For example, electricity generation investment in Crete helped support and maintain a nine percent growth in demand, which itself was a reflection of the growth of tourism, a sector of high labour intensity. The rapid and widespread introduction of mobile telephony across the country has reportedly provided major incentives for new or expanded businesses in all regions.

A reduction in employment has occurred in projects that increased production efficiency, because capital has usually substituted labour. This was the case in the railway and port projects as well as in the ‘crash programme’ to restructure and modernise the fixed-line telecommunications system. Nevertheless, in a broader perspective, an increase in production efficiency usually strengthens a company’s, a region’s and the country’s overall competitiveness. For example, the fixed-line telecommunications company can now compete with the best in Europe and has already invested in a wide variety of profit-making and employment-creating subsidiary activities, in both Greece and elsewhere.

In conclusion, the information available suggests a very limited long-term direct employment creation effect of the projects financed by the Bank, partly because so much of the portfolio consists of infrastructure projects where the indirect effects are considered more important. Whether the Bank has had a significant impact on the general level of employment cannot be verified by evaluations based on projects which have been operational for a couple of years only. Direct and indirect employment effects are better evaluated by impact studies usually carried out much later than typical ex-post evaluations. As mentioned already, these are very labour-intensive and beyond the scope of the present report.

³³ The two water supply and sewerage projects created 62 new jobs, of which 43 were expected to be permanent.

3.7 Impact on the Environment

All appraisal reports for the 49 projects that were not global loans included a review and description of the potential environmental impacts of the projects concerned, their compliance with the relevant EU Directives, where appropriate, and mitigation measures undertaken or planned. For one road project environmental mitigation measures and monitoring procedures were exemplary and could be used as benchmark indicators for other projects. Furthermore, the costs of the mitigation measures were included in total project costs. However, most external environmental costs such as air or sea pollution and visual impact, as well as benefits such as improved water supply or drainage, were identified but not quantified.

For several types of projects, especially large and costly ones, an Environmental Impact Assessment (EIA) is mandatory under EU Directive 85/337. Although Greece had an exemption from this directive for most of the period under review, EIAs were indeed undertaken. In other cases, such as water and sewerage projects, the Bank required other types of environmentally related studies. These were also done. In all cases, the EIA or similar study was carried out during project implementation rather than as part of the preliminary preparation. This appears to have been appropriate, even if some delays were caused to project implementation, as the mitigation measures eventually required could, as expected, be appended to the project design without seriously affecting the overall project.

Whether the local population was adequately informed about, consulted on and, if appropriate, compensated for the potential impacts of a project on their environment seems to have depended largely on the project promoter. For instance, many road projects were delayed because of disputes with landowners about expropriation. Conversely, in other sectors, disputes were avoided through generous compensation and mitigating measures.

3.8 Conclusion: Outcome of Project Selection in Greece 1989-2000

Among the 56 projects reviewed, in the evaluators' opinion:

- 30 were good projects; of which 21 were satisfactorily implemented and put into operation (10 electricity projects, 6 telecommunications projects, 4 transport projects and 1 global loan) and nine faced subsequent problems that could not be foreseen at the time of appraisal (4 global loans, 4 transport projects and 1 electricity project);
- 11 should not have been selected without substantial changes to, or clarification of, design (5 transport projects, 3 electricity projects and 3 framework loans) or institutional set-up (the 3 electricity projects). Eight had other serious problems, which should have been dealt with before selection (6 transport projects, 1 electricity project and 1 other infrastructure project);
- 7 should not have been selected at all as they faced severe problems that should have prompted a complete review of the projects (2 global loans, 2 transport projects, 2 other infrastructure projects and 1 framework loan).

At the time of appraisal, 30 of the 56 projects met what should be the Bank's standards of relevance, cost-efficiency, sustainability and profitability. However, in retrospect, 9 of the projects that faced problems when appraised by the Bank eventually turned out, in the evaluators' opinion, to have a good or satisfactory outcome both in terms of operational success and impact on regional development. In total, 39 projects (i.e. 70% of total) were ultimately acceptable on both counts³⁴.

There is no distinct time pattern in the quality of projects over the 56 evaluated: it is not possible to say that more recent projects have performed better or worse than older ones.

³⁴ The four direct lending projects of 1989 that were not reviewed in detail all turned out to be poor projects facing very severe implementation problems according to their Project Completion Reports.

4 Selection Indicators and Criteria

4.1 Indicators and Criteria Used, 1989-2000

The Bank follows the EU approach to give priority to projects located in assisted areas. From a theoretical point of view, various refinements are possible to measure the contribution of a project. During the period under evaluation, the Bank recognised that indicators were needed to assess its impact on regional development. The Bank therefore presented a paper to its Board in 2001 proposing performance indicators for regional development projects. It recommended a three-pronged appraisal of projects:

1. checking the technical, economic, environmental and financial qualities of the project - and in particular ensuring a satisfactory economic and financial rate of return;
2. assessing how, and how much, the project contributes to regional development;
3. highlighting the financial advantages that the Bank's intervention can have for those concerned.

In order to assess the project's contribution to regional development, the paper recommended a further three steps:

1. checking that the project is newly located in an assisted area (and is not a relocation from one assisted area to another);
2. ensuring that the project is consistent with the EU structural programmes and that it contributes to addressing some obstacle to growth that exists in the region;
3. calculating indicators whenever possible.

These proposals, which relate to all Objective 1 regions in the EU, are under implementation and the format of the project appraisal and Board reports should soon change accordingly.

This evaluation adds two elements to the debate:

- It is clear that there is no single universal and unambiguous indicator of regional development. There is a need to increase awareness among staff about the problems and issues of regional development and its objective of contributing to convergence. It is not sufficient for Board reports simply to state that the project is located in an assisted area, and therefore eligible for financing under regional development. There should be a reasoned, and at least qualitative, explanation of the contribution of the project to regional development.
- Second, as long as there remains the need for stricter project appraisal discipline these refinements remain second-degree improvements, as the evaluation has illustrated. Indeed, as already noted, potential selection indicators, such as the ERR, have sometimes been disregarded when they argued against selection, which was easy to do in the absence of a clear ERR benchmark. Moreover, the selection criteria for the less relevant, sustainable or profitable projects appear to have been based on the speed and ease with which

a project loan could be processed and signed (and therefore the number of loans which could be signed each year). It is also probably the case that between two project loans with similar speed and ease of processing and signing, the larger one would be selected.

Of course the same selection indicators and criteria were used for relevant, cost-efficient and profitable projects. However, the striking difference is that all these projects were properly prepared, well justified, part of prioritized investment programmes based on realistic demand forecasts, and to be built and managed by competent and experienced project promoters who were well-known to the Bank.

The portfolio could have been improved to the benefit of both Greece and the Bank if appropriate selection criteria had been used effectively.

4.2 Regional Development Indicators

One of the main objectives of this evaluation has been to identify measures that would have strengthened the Bank's impact in Greece. One measure would have been to develop and adopt appropriate indicators and criteria for the selection of 'regional development' projects in the EU, i.e. projects that help bring the average income in the region closer to the EU average. The use of Greece as an example has both advantages and disadvantages in this respect, since the whole country is eligible for regional development loans. The advantages are, first, that the indicators and criteria can draw on the country's national investment programmes and priorities in its own attempts to promote convergence and, second, that they would be applicable to potential projects in "accession countries" likely to join the EU in the coming years. The main disadvantage is that the indicators would not necessarily be applicable to the more usual meaning of 'regional development', i.e. the lessening of income disparities within the EU member countries. Therefore, it must be clear that what is discussed in this section is only applicable to Objective 1 countries.

In principle, the selection indicators and criteria should be applicable to all types of potential projects in the Bank's portfolio to enable inter-project comparisons to be made. There are many different types of project, the main ones in Greece being:

- Revenue-earning infrastructure projects, whether state-owned, privately-owned or of mixed ownership;
- Non-revenue-earning infrastructure projects, usually owned by the state or local authorities;
- Commercial investment projects, again state-owned, privately-owned or of mixed ownership;
- Framework loans, covering a large number of small projects, provided to commercial entities, the state or local authorities; and
- Global loans, for on-lending to SMEs, provided to state-owned investment banks, domestic- or foreign-owned commercial banks or other types of financial intermediaries.

The selection indicators and criteria should, other things being equal, also enable the EIB to ensure consistency of project selection with the EU's policies and Directives,

as well as with the EU's own financial participation (grants) in projects in the Objective 1 regions through the Cohesion Fund and other funds.

Projects that have, at least, an ERR or net benefit which is higher than for similar projects in other parts of the EU, as well as the opportunity cost of capital (in real terms) in Greece, contribute to bringing the average income of the Objective 1 region closer to the EU average. However, as has already been seen, an ERR or net benefit cannot always be realistically calculated on a sound methodological basis. In some of its project appraisals, the EIB has used surrogate measures, such as unit investment or production costs. For other projects, more subjective criteria have been applied.

4.3 A stricter Appraisal Discipline for Regional Development Projects

As stated above, the 56 projects evaluated in Greece have shown that there is no single and unambiguous selection indicator for comparing all the different types of regional development projects. Nor is there any single criterion (or test) that can be applied. However, it is certainly feasible to devise and apply a rational selection strategy designed to promote convergence and based on a series of criteria that all projects must meet if they are to be selected.

The EIB's experience in Greece since 1989 has shown that certain types of projects financed by the Bank were fully justified i.e. relevant, sustainable, cost effective and profitable:

1. Projects in revenue-earning infrastructure sectors, such as electricity and telecommunications, for which detailed sector studies had regularly been carried out (by the Bank or other competent agencies) and for which a prioritised staged investment programme had been developed by competent management based on realistic demand forecasts.
2. Projects in non-revenue-earning infrastructure sectors, such as transport, for which detailed technical, economic and financial feasibility studies had been undertaken and which would be implemented by competent and experienced promoters;
3. Projects promoted by competently managed private sector enterprises, such as mobile telephone companies, as part of their investment and expansion plans to raise overall profitability.
4. Global loans to experienced financial intermediaries with a good record of medium-term lending to private sector SMEs and satisfactory credit risk analysis and project supervision procedures.
5. Framework loans in both revenue-earning and non-revenue-earning infrastructure sectors for which the majority of small sub-projects had been clearly identified, justified and prioritised and which would be managed and supervised by a competent promoter with appropriate monitoring facilities.

On this basis, the following combination of clear, unambiguous and easily understandable selection criteria for directly financed projects would make up an appropriate selection strategy:

- Step 1: For any project for which a methodologically sound ERR can be calculated, the ERR should be at least higher than the opportunity cost of capital (in real terms) in Greece. For any project for which a surrogate cost-based measure for ERR is used, such as unit investment or output costs, this should be equal to or lower than those for similar projects elsewhere in the EU.
- Step 2: The project should be based on competent and detailed sector studies, undertaken or approved by the Bank, and should be of high priority in the investment programme for the sector. It should be dimensioned in line with realistic expectations about future demand or use and should be cost-efficient.
- Step 3: The project should be properly prepared in terms of detailed technical, financial and economic feasibility studies. It should be at an early enough stage of design or preparation for the Bank's technical and/or economic staff to have sufficient input to ensure the success of the project.
- Step 4: The project promoter should be appraised to confirm his competence, experience and capacity to implement the project as well as to ensure that he is fully aware of the Bank's project selection criteria.
- Step 5: The project should be technically, economically, financially, and environmentally sustainable in the medium to long term. Objectively verifiable indicators should be established to provide an early warning of unexpected problems materialising during project implementation. If the project is also receiving financial (grant) support from the EU, the Bank should be assured that this would not affect the viability or sustainability of the project.
- Step 6: The project should not suffer from uncertainties about the institutional framework including asset ownership, the regulatory framework or other legislative issues.
- Step 7: The project should have no severe adverse environmental impact, or, if it does, must incorporate appropriate mitigating measures.
- Step 8: The project should comply with all relevant EU Directives on environment, procurement, employment, competition, etc.

Two of these steps are not part of the Bank's standard appraisal practice: step 2 (sector studies) and step 6 (institutional and regulatory analysis). They are incorporated because the evaluation has shown, especially in the transport and other infrastructure sectors, the weaknesses of project identification and selection, which is not based on broader sector analysis. The review of the portfolio has also illustrated gaps in the Bank's portfolio in the priority sectors for lending in Greece. Furthermore, the evaluation came across cases of weak institutional aspects in which, even if step 6 was indeed carried out and proved useful, it did not help prevent problems that materialised.

While the other steps are standard in the Bank's appraisal procedure, the evaluation has pointed out weaknesses in the way steps 1 (profitability), 3 (review of project design), 4 (promoter's project management skills) and 5 (sustainability) have been performed for some projects. This suggests the need for stricter appraisal discipline in future. Discussions with the services have highlighted that the recommendation of a more rigorous appraisal approach was not specific to projects in Greece, although it is particularly important where the pool of projects on offer is mixed, with some large projects presenting design or institutional weaknesses. This recommendation is fully consistent with, and indeed complementary to, the current development of more upstream/sector work in the Bank to help define its role as a "Policy Bank".

The selection criteria for framework loans should be that all component sub-projects are clearly defined, justified, prepared and prioritised and the Bank should be confident that these sub-projects would be competently managed and monitored³⁵.

The selection criteria for global loans should be that they are only made to competent financial intermediaries, experienced in medium-term lending to SMEs and with appropriate credit risk analysis and project supervision systems in place.

A proposed directly financed project that does not meet all eight selection criteria may still be regarded as 'marginal', with a high potential for selection if appropriate remedial measures are undertaken before the loan is signed. One further set of important criteria for determining this includes:

1. If the project promoter can be persuaded to redesign the project in such a way as to remove the negative aspects and thereby increase the ERR or surrogate measure to an acceptable level.
2. If appropriate justification for the project can be provided in the context of a prioritised national, regional or sector investment plan.
3. If the promoter can provide the additional detailed technical, financial and economic information required by the Bank.
4. If the promoter can substantially strengthen the project management team and adopt acceptable procurement procedures.
5. If the promoter can provide greater assurances about the technical, economic, financial, fiscal and environmental sustainability of the project and provide objectively verifiable indicators for monitoring.
6. If uncertainties about asset ownership, the regulatory framework or other legislative issues can be resolved before the loan is signed.
7. If mitigating measures can quickly be put in place to offset any adverse environmental impact.

A second set of criteria, which is outside the framework of normal banking practice and relates to broader regional development issues, comprises (usually) unquantifiable factors which might, in certain cases, legitimately more than compensate for minor failures of 'marginal' projects in meeting one or more of the selection criteria. This set includes:

³⁵ A recent statement by the Bank on 'Handling of Investment Programmes (Programme Approach)' provides similar project-related and promoter-related criteria for the use of framework loans (though they are not called framework loans in the statement).

1. If the project makes a substantial contribution to improving the environment in the region.
2. If the project makes a substantial contribution to improving the competitiveness of the region.
3. If the project is likely to improve economic welfare in the region through changes in income and wealth distribution.
4. If the project itself provides substantial new permanent employment in a relatively depressed area.
5. If the project is likely to provide the incentive for substantial creation of new or linked enterprises in the region.
6. If the project transfers technology of high EU specification and standards to the region.
7. If the project attracts new research and development facilities or new technologies to the region.
8. If the project is likely to strengthen the banking and financial activities in the region.

4.4 ‘Testing’ the Selection Strategy in Greece

If this selection strategy had been in operation for the EIB’s lending to Greece during the period 1989–2000, the 26 projects that lacked either relevance, sustainability or profitability would not have been selected as proposed. Seven would not have been selected at all and of the other 19, perhaps 16 could be regarded as ‘marginal’ with a reasonably high potential for the promoters to ensure that all selection criteria were fully met before the loan was signed. For the other three projects, the only hope for eventual selection would have been substantial redesign, probably involving considerable delays.

Note that all 30 of the projects appraised according to the proposed strategy have been evaluated as good or satisfactory projects. Very few of them faced difficulties (and these, when occurring, turned out to be temporary). Of the 26 projects that, in the opinion of the evaluators, have not been rigorously appraised, only nine can be considered relevant, sustainable and profitable projects, i.e. a 35% success rate. Eliminating seven poor projects from the portfolio would have already increased the overall success rate from 70% (39 out of 56) to 80% (39 out of 49).

While the implementation of the strategy would increase staff input in some areas (e.g. sector work), it is by no means certain that the overall result would be an increase in staff workload, given staff saving later in the project cycle. The absence of strict appraisal discipline is itself very costly: several projects were appraised three times and required years of negotiations. The monitoring of poor projects is also more time-consuming, both for lending and for technical staff. Ensuring good project selection and strict appraisal discipline is one way of reducing project processing and monitoring work later, thus freeing resources for further useful lending.

THE EUROPEAN INVESTMENT BANK

The European Investment Bank (EIB) is owned by the fifteen European Union (EU) Member States and has its headquarters in Luxembourg. It supports EU policies on a self-financing basis, raising its resources on the world's capital markets for onlending to sound capital investment projects that promote the balanced development of the European Union.

Set up in 1958 by the Treaty of Rome, the EIB has its own administrative structure and decision-making and control bodies (Board of Governors - usually the Finance Ministers of the Member Countries - Board of Directors, Management Committee and Audit Committee).

As a major international borrower, which has always been awarded the highest "AAA" credit rating by the world's leading rating agencies, the EIB raises large volumes of funds on fine terms; it onlends the proceeds of its borrowings on a non-profit basis.

The volume of the EIB's operations has grown steadily and the Bank is today one of the largest financing institutions of its kind in the world. While the bulk of its loans are within the European Union, the Bank has also been called upon to participate in the implementation of the Union's development aid and cooperation policies through financing for the benefit of some 120 non-EU countries. It therefore supports:

- Economic growth in the African, Caribbean and Pacific States and the Overseas Countries and Territories, as well as in the Republic of South Africa;
- A stronger Euro - Mediterranean partnership;
- Preparations for the accession of the Central and Eastern European Countries and Cyprus;
- Industrial cooperation, including the transfer of technical know-how, with Asia and Latin America.

The EIB began carrying out ex-post evaluations in 1988, mainly for its operations in non-EU Member Countries. In 1995, the Bank established an Evaluation Unit to cover operations both inside and outside the Union. Ex-post evaluations take a thematic approach and are intended for publication. To-date the bank has published:

1. Performance of a Sample of Nine Sewage Treatment Plants in European Union Member Countries (1996 - available in English, French and German)
2. Evaluation of 10 Operations in the Telecommunications Sector in EU Member States (1998 - available in English, French and German)
3. Contribution of Large Rail and Road Infrastructure to Regional Development (1998 - available in English, French and German)
4. Evaluation of Industrial Projects Financed by the European Investment Bank under the Objective of Regional Development (1998 - available in English, French and German)
5. An Evaluation Study of 17 Water Projects located around the Mediterranean (1999 - available in English, French, German, Italian and Spanish).
6. The impact of EIB Borrowing Operations on the Integration of New Capital Markets. (1999 – available in English, French and German).
7. EIB Contribution to Regional Development A synthesis report on the regional development impact of EIB funding on 17 projects in Portugal and Italy (2001 – available in English (original version), French, German, Italian and Portuguese (translations from the original version)).
8. Evaluation of the risk capital operations carried out by the EIB in four ACP countries 1989-1999 (2001 - available in English (original version), French and German (translations from the original version)).
9. EIB financing of energy projects in the European Union and Central and Eastern Europe (2001 - available in English (original version), French and German (translations from the original version))
10. Review of the Current Portfolio Approach for SME Global Loans (2002 – available in English (original version), French and German (translations from the original version)).
11. EIB Financing of Solid Waste Management Projects (2002 – available in English (original version), French and German (translations from the original version)).
12. Evaluation of the impact of EIB financing on Regional Development in Greece 2003 – available in English (original version)).

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