



**Operations Evaluation**

**AN EVALUATION STUDY  
ON INDUSTRIAL PROJECTS  
FINANCED BY THE  
EUROPEAN INVESTMENT BANK  
UNDER THE OBJECTIVE  
OF REGIONAL DEVELOPMENT**

Based on reports made on behalf of the European Investment Bank by

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## The EIB and Regional Development

The objective of reducing disparities in growth rates between the regions is enshrined in the fifth recital to the Treaty establishing the European Community:

“Anxious to strengthen the unity of their economies and to ensure their harmonious development by reducing the differences existing between the various regions and the backwardness of the less-favoured regions”.

However, in order to avoid distorting competition between Member States, the Treaty sets out a very strict framework for possible forms of regional development aid.

The Treaty explicitly entrusts the EIB with the remit of supporting regional development: “The task of the European Investment Bank shall be to contribute...to the balanced and steady development of the common market... For this purpose the Bank shall.... Facilitate the financing of ... projects for developing the less-developed regions” (Article 130 of the Treaty of Rome superseded by Article 198e of the Treaty on European Union – 1992).

Until 1975 and the creation of the European Regional Development Fund (ERDF), managed by the European Commission, the EIB was virtually the sole source of Community financing for regional development projects.

The dawn of the ERDF represented a significant stage inasmuch as it ushered in substantial, direct contributions from the Community budget in the form of grant aid, a development that in no way undermined the importance of the EIB’s input.

Over the years, a variety of additional Community objective mandates have been handed down to the EIB, including that of helping to improve communications between the Member States. Nonetheless, regional development has consistently ranked foremost, with almost two-thirds of aggregate annual financing given over to the least-favoured countries.

In 1988, reform of the Structural Funds introduced a new distinction between the different levels of regional development in terms of “Objective” classifications. The main category was labelled “Objective 1” and embraces all regions recording average per capita income 75% below the Community average<sup>1</sup>.

Adoption of the Single European Act served to speed up the process, according unequivocal priority to the aim of strengthening the Community’s economic and social fabric. At the same time, the go-ahead was given to doubling the Structural Fund’s budgetary appropriations, with the proactive partnership of the EIB.

The Treaty on European Union (the Treaty of Maastricht) gave the EIB increased responsibilities in the drive towards greater economic and social unity.

These responsibilities encompass:

1. direct contributions towards financing capital projects in areas eligible for assistance under the Structural Funds (Objectives 1 – 2 and 5(b));
2. operations in areas covered by other specific support measures promoted by the European Union;
3. infrastructure financing having an indirect impact on regional development.

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<sup>1</sup> Regional objectives:

Objective 1:	Economic adjustment of regions whose development is lagging behind
Objective 2:	Economic conversion of areas affected by industrial decline
Objective 5(b):	Economic diversification of vulnerable rural areas
Objective 6:	Development of areas with an extremely low population density

The purpose of this report is to provide a clearer insight into how the third category of activity serves to foster regional development.

The study is one of three offering an evaluation of the impact on regional development of investment in major road and rail infrastructure, telecommunications and industry.

Note: In community parlance and in contrast to other multilateral development agencies, the term "region" denotes an entire country or parts thereof rather than an area encompassing several countries. In its Nomenclature of Territorial Units for Statistical Purposes (NUTS), the Community adopts three subdivisions. In most cases, "region" falls within the NUTS 2 subdivision, generally considered the most important in economic terms.

Correlation between NUTS and national administrative subdivisions:

	<b>NUTS 1</b>	<b>NUTS 2</b>	<b>NUTS 3</b>
Belgique/België	Régions	Provinces	Arrondissements
Danmark			Amter
Deutschland	Länder	Regierungsbezirke	Kreise
Ellada	NUTS 2 groupings	Development regions	Nomoi
España	NUTS 2 groupings	Comunidades autónomas	Provincias
France	ZEAT + DOM	Régions + DOM	Départements + DOM
Ireland			Planning regions
Italia	NUTS 2 groupings	Regioni	Provincia
Luxembourg			
Nederland	Landsdeien	Provincies	COROP-Regio's
Österreich	Gruppen von Bundesländern	Bundesländer	Gruppen von Politischen Bezirken
Portugal	NUTS 2 groupings	Comissões de coordenação regional + Regiões autónomas	Grouping of cancelhos
Suomi/Finland	Manner-Suomi Ahvenanmaa	Suuralueet	Maakunnat
Sverige		Riksomraden	Län
United Kingdom	Standard regions	NUTS 3 groupings	Counties, local authority regions

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## EXECUTIVE SUMMARY

### Introduction

- The present evaluation study was launched to examine how industrial projects financed by the European Investment Bank were contributing to regional development in the member countries of the European Union.
- The study evaluates the quality of the investments in terms of their implementation and operational performance and attempts to assess EIB's contribution to European Union objectives with particular emphasis on regional development.
- The study covers industrial projects financed directly by the EIB. This type of operation declined as a percentage of EIB lending from around 10%, in the late 1980s and early 1990s, to close to 5% over the 3-year period 1994-96; in 1997 it bounced back to 12%. This downward trend, if confirmed, could reflect increased competition in the banking sector and suggest that the EIB has been placing greater emphasis on financing infrastructure.
- The study was carried out in two stages:
  - (i) a desk review of the implementation completion reports<sup>1</sup> of 76 operations (called P76 in what follows);
  - (ii) field evaluations of 15 operations (P15 drawn from P76) by three independent, external consultants.
- The P15 sample was selected by the Evaluation Unit to maximise coverage of sector, geographical location, as well as size and type of investment, rather than to be statistically representative of EIB's overall industrial portfolio.

### Conclusions

#### Project Implementation

As far as physical implementation of the investments is concerned, there was a considerable degree of consistency between the findings of P76 and P15. They show that the industrial projects financed by the EIB are generally well implemented.

Whenever project design was changed in the course of implementation, alterations were well managed and adapted to evolving market conditions. Investment cost and implementation duration deviated only moderately from forecasts. Initial financing of the investments was sound, reflecting the high standing and quality of the promoters.

The data in the implementation completion reports (ICRs) varied in terms of completeness. Project monitoring and completion reporting were basically geared to verifying contractual conformity and controlling EIB credit risk. Reporting on project outcome was limited, and aspects such as performance, employment, environment, etc. were frequently difficult to compare with initial estimates.

#### Project Performance

Technically, projects were found, with few exceptions, to be operating successfully. Commercial performance was less uniformly satisfactory underlining the fact that for industrial lending, marketing is a key success factor and merits careful scrutiny. Financial results were unsatisfactory in four P15 cases, mainly as a result of commercial difficulties. The proportion of financial deficiencies was larger in P15 than in P76: between implementation completion (P76) and evaluation (P15), a number of projects undoubtedly performed less well than expected, in some cases due to the adverse economic conditions prevailing in Europe in recent years. It must be noted, however, that in none of these cases did financial deficient projects entail a loss on loans made by EIB.

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<sup>1</sup> The implementation completion report (ICR) is drawn up for internal monitoring and control purposes at the end of the implementation phase.

In several instances, the physical project approach<sup>2</sup> made it difficult to determine project benefits and related effects (cash flow, jobs, environmental impact, etc.). In a number of cases, *ex-ante* profitability had not been calculated and for no project was it verified at the end of the implementation period.

### Project Impact

In P76, reported employment creation exceeded appraisal expectation and evaluation results in P15. The study suggests that large industrial projects financed by the EIB have only a modest impact in terms of direct job creation. The report does not attempt to assess indirect employment impact, which may be more significant.

The EIB assumes that any industry located in a less advanced area will contribute to regional development. While this may often be the case, other interests may have justified the location in such an area. Hence, to measure impact on regional development, the study applied, on an experimental basis, a set of criteria designed to indicate the relevance of such projects to the regional economy (Annex 3). While P76 provided little explicit data allowing impact assessment, 7 projects in P15, contained clear evidence of a favourable local impact; 4 more were likely to have had a positive effect but there was little concrete proof to back up this assumption; and finally, 4 were unlikely to have made any significant contribution to the local economy.

The experimental use of such criteria shows that, although the methodology needs further adjustment, the approach is a helpful tool in assessing regional development impact and could usefully be applied starting at the time of appraisal.

### EIB's Contribution

Most P15 project promoters acknowledged that competitive interest rates and loan maturities represented the principal attractions of EIB financing; some also mentioned that the Bank's intervention enabled them to obtain complementary finance on more favourable terms (seal of approval).

The general impression of successful projects promoted by well-managed, large industrial companies with adequate financial resources, raises the complex issue of subsidiarity<sup>3</sup>. Promoters stated that the investments would have been implemented even without the EIB, but its loans on truly competitive terms were regarded as an important contribution to projects' successful realisation and, in that sense, were seen as a source of "value-added". Further consideration should be given to this, for example, by systematically introducing relevance indicators enabling EIB to better demonstrate the geographical distribution of the benefit of its operations.

The study indicates that the EIB should develop its knowledge of clients and operations, including an information system providing knowledge of past practices to improve future operations. While EIB's credit risk monitoring is highly developed, its project monitoring is weak or non-existing, in particular after implementation completion. Furthermore, project definitions are often unclear and feedback from promoters on project performance inadequate.

The EIB was found to be in need of an up-to-date industrial lending strategy; concentration on lending volume seems in various cases to hamper the pursuit of clients' needs. With a limited range of financial products available, such a strategy seems necessary especially with regard to promoting European industrial competitiveness. In this context, the EIB should contemplate increasing in its industrial loans portfolio the share of smaller, probably more risky undertakings which have less ready access to the international capital markets<sup>4</sup>.

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<sup>2</sup> Some "Projects" were defined as a collection of fixed assets neither geographically nor functionally linked.

<sup>3</sup> Art. 18 of EIB's Statute : "...the Bank shall grant loans...for investment projects..., to the extent that funds are not available from other sources on reasonable terms." was conceived at a time (1957) when capital markets were far less developed than now and EIB enjoyed a unique position in this context.

<sup>4</sup> An important step in this direction was taken with the Amsterdam Special Action Programme decided in June 1997, covering amongst others a new SME "window" enabling the EIB in co-operation with the European Investment Fund (EIF) to make risk funds available to innovative enterprises.

A new approach to the financing of industrial projects is required for the EIB to make the best use of its resources, maximise its impact on European objectives, and adapt to a rapidly changing financial environment which is bringing the EIB much closer to other banks and financial institutions in terms of both co-operation and of competition.

### Recommendations

On the basis of the analysis and reporting provided by the consultants the following main recommendations were retained. Reactions and responses of the EIB are also recorded:

Recommendations	EIB Response
Monitoring and completion reporting should be strengthened. Industrial projects should be subject to completion reporting only when they have been operating for a few years to allow a better assessment of their performance. The whole monitoring process should place greater emphasis on clients.	The EIB is carrying out a fundamental restructuring of its project monitoring activities, which seeks to attain a balance between available resources and monitoring requirements.
Marketing and management flexibility are key factors in determining industrial projects' financial success. Appraisal teams should pay particular attention to the promoters' commercial and management capabilities.	The EIB accepts this and is already devoting more attention to these aspects. Project appraisal and monitoring services were restructured in 1995 creating a closer link between project engineers and economists.
The EIB should revise its approach toward physical investments and define projects primarily in terms of a comprehensive, quantified description of the project's purpose in the context of the promoter's overall capital expenditure plans.	The EIB has started to substitute programme for project lending. Moreover, the question of how to reconcile project finance and corporate finance is currently a subject of internal reflection within the EIB.
The EIB should harmonise the presentation of financial statements of its industrial clients in line with EC Directives in this regard.	National legislation is still applied by EIB clients and imposing a single format in present circumstances would unduly raise transaction costs.
For industrial projects eligible for EIB financing under regional development, the Bank should introduce systematically at appraisal a set of relevance criteria to assess impact on regional development. Such indicators would help the EIB demonstrate "value-added".	The Projects Directorate has undertaken to test such criteria in key sectors, including industry.
A review of EIB's strategy is recommended aiming at maximising the impact of its industrial lending.	In view of the changing environment and in response to this recommendation, EIB staff has undertaken to examine the options available and the strategic implications of a reorientation in terms of industrial lending, while taking into account resource constraints.

## 1. PURPOSE, BACKGROUND AND METHODOLOGY

The present evaluation study was launched in May 1996 as part of a programme designed to verify the contribution of the EIB to its priority goal of regional development, through its lending operations in the sectors of telecommunications, large road and rail infrastructure and industry. It was confined to industrial projects located in the member countries of the Union, and financed under individual contracts<sup>5</sup>.

<sup>5</sup> Global loan operations i.e. financing of small and medium enterprises through financial intermediaries,

The share of individual loans to industry aimed at furthering regional development has fluctuated over the years and dropped over the recent past (table 1.1) compared to an average of 10% in the 1980s. Several factors may have influenced this development, such as cyclical business conditions, increased competition from commercial banks, the growing relative importance given to infrastructure financing including large-scale schemes such as the Edinburgh facility and TENs initiative. Moreover, being a relatively small item in the overall EIB portfolio it may also have been substantially influenced by single, large-scale operations that boosted its percentage share in certain years.

<b>ECU million</b>	<b>1993</b>	<b>1994</b>	<b>1995</b>	<b>1996</b>	<b>1997</b>
<b>EIB total</b>	16597	16386	17569	19788	21847
<b>Individual loans to Industry for Regional Development</b>	2215	1207	1034	1055	2602
<b>in percent</b>	13	7	6	5	12

The study was carried out in two stages:

- on the basis of information available in-house and mainly in the so-called Implementation Completion Reports (ICR)<sup>6</sup>, examination of a selection of 76 operations implemented during the period 1988-1993 (denominated P76 in what follows) representing about 25% of all such projects financed since 1985;
- in depth evaluation of a sample of 15 operations, extracted from P76 to provide as faithful as possible a cross-section of the Bank's industrial operations<sup>7</sup>.

External consultants carried out the second stage of the study through site visits and meetings with promoters. Data collection was facilitated by questionnaires<sup>8</sup> sent to promoters in advance of consultants' visits.

The study required some 320 EIB staff-days and 150 consultant-days.

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although an important vehicle for EIB financing of industry, are of a different nature and therefore excluded here. Direct lending to industry represents about half the targeted portfolio.

<sup>6</sup> The ICR is the document which examines conformity with the promoter's contractual commitment to carry out a project as described in the finance contract.

<sup>7</sup> Although 2 projects of those originally chosen were replaced at the request of the operational services, the sample appears to reflect EIB's operations in this field.

<sup>8</sup> See model questionnaire (adapted to suit the individual projects) in Annex 1.



## 2. SUMMARY OF FINDINGS ON 76 INDUSTRIAL OPERATIONS

### 2.1 Population Characteristics

P76 covers a broad range of manufacturing industries giving a fair representation of EIB financed industrial projects in the Union.

	Number of Projects	% of Investment Cost <sup>9</sup>
Chemical Industry	23	26
Transport Equipment	7	20
Electrical and Electronics	11	17
Pulp, Paper, Printing	9	12
Miscellaneous other	25	25
Total	76	100

Each Union member country is also represented but more than half of the portfolio is located in Italy.

The Italian authorities' support for industrial borrowings in assisted regions through exchange risk and credit guarantees as well as the presence of an EIB department in Rome may have contributed to this.

Size-wise, P76 reflects EIB's tendency to favour large projects (average 103m ECU, median 66m ECU - table 2.2). Even the eight smallest projects (10% of P76) show an average cost of 18.8m ECU, corresponding, by most industrial standards, to a sizeable investment.

M ECU	0-25	25-50	50-75	75-125	125-200	200-500	500-1000	1000 -	Sum
Projects	7	23	15	17	7	5	1	1	76
Average outturn cost	19	38	64	92	141	326	581	1124	103
% of total	1.6	11.1	12.2	20.0	12.6	20.8	7.4	14.4	100

As many as 54 projects (70%) were composite investments forming part of a wider investment plan or programme. As few as 12 (16%) were greenfield operations, the rest being extensions or modernisations.

### 2.2 Conformity of Implementation with Initial Plans

With only one exception, implementation of the 76 projects was devoid of any major technical problems regarding project design. EIB's selection process is strict and only projects that are technically viable pass the admission test.

<sup>9</sup> In what follows, investment cost is given in ECU and defined as outturn project cost in fixed 1995 prices. Local currency amounts, as recorded at the time of the ICR, were inflated into 1995 prices and then converted into ECU.

Nonetheless, a substantial number of projects were altered in the course of realisation: this is common in an industrial environment where survival depends on adaptability. Design modifications did not seem to impact negatively on the operating capabilities of the projects: 60 projects (79%) were reported as complying with initial plans in respect of production and capacity, and only one project was seriously deficient.

The promoters' expected rigorous approach to project implementation is corroborated by the small deviations in terms of duration and costs. About half the projects came on stream more or less on time while 2 were so severely behind schedule as to incur serious problems. Minor delays with the remainder could be justified by necessary changes in the original plans. Eight of the 76 projects suffered substantial cost overruns (i.e. over 30%), and 58 projects were close to their target (less than 10% overrun).

### **2.3 Operational Performance**

At project appraisal, average financial return was estimated at around 20%, and only 9 projects were expected to yield a profitability below 12%. However, in 11 cases a rate of return was not calculated at appraisal because projects were part of larger schemes or programmes, and it was deemed impractical to determine their contribution to earnings.

At the ICR stage, there was no recalculation of the rate of return for any project. However, by examining information available on developments in relevant project parameters, and by making a comparison with the promoter's overall financial performance, it was possible in most instances to estimate whether profitability outcome was satisfactory.

An acceptable 6 projects (8%) turned out to be financially deficient, while 33 projects (43%) did not live up to initial expectations but their profitability was still viewed as acceptable. Not surprisingly, commercially successful projects were also reported as profitable.

There seems to be little connection between project outturn cost and financial performance: 7 of the 8 projects which suffered substantial cost overruns all presented an acceptable financial result, while the 6 financial failures showed a satisfactory cost outturn.

### **2.4 Impact**

Implementation Completion Reports did not assess the impact on regional development. Indeed, since there was rarely any reference at appraisal to the intended regional development impact, it was impossible to carry out a meaningful verification at the end of the investment stage.

The only impact element dealt with in most of the ICRs was employment with results proving better than estimates: more jobs were created by those projects having a positive employment impact, and fewer jobs eliminated by those with a forecast negative one.

Job-creating projects were generally the larger ones, undoubtedly those providing new production capacity. Modernisation projects would a priori not be expected to create additional employment.

### **3. EVALUATION OF 15 INDUSTRIAL PROJECTS**

#### **3.1 Sample Characteristics**

Basic characteristics of the 15 projects are presented in Annex 2.

They were selected so as to ensure the best possible representation of the EIB's industrial portfolio. Distribution by both sector and size is therefore close to that of P76. Projects were also selected to cover the broadest possible geographical range: the 15 projects were located in 10 EU countries.

The P15 projects were about 10% larger than those of P76: average P15 size was 114.0m ECU, the median of the sample 76.5m ECU. The two biggest projects together account for 34% of total investment costs.

Seven projects in P15 involved composite, largely unconnected investments at more than one geographical location, and 2 further projects comprised investment items situated at the same location but functionally disconnected. In the case of such composite projects it proved difficult at the evaluation stage to retrace individual parts, and the findings therefore necessarily involve some uncertainty.

#### **3.2 Conformity of Implementation with Initial Plans**

##### **3.2.1 Project Design**

Eleven of the 15 projects were significantly altered in terms of technical design during the implementation period. However, most modifications were prompted by the rapidly changing commercial and technical environment, and projects largely preserved their ability to manufacture the products in the quantities and qualities specified in the initial plans. Capacity was deliberately reduced in only 2 cases.

##### **3.2.2 Implementation Cost**

Average project cost planned was 104.4m ECU, whereas at outturn it was 114.0m ECU, an increase of 9.3%, largely explained by physical changes.

Four out of 5 significant cost increases were basically due to important additional investments introduced during the implementation period to benefit from, or adapt to, unexpected new market opportunities. In the fifth case, a cost overrun was incurred partly because of unforeseen technical difficulties.

Four projects whose cost turned out lower than planned, had all been reduced in physical terms, 2 because of disappointing market prospects, and 2 following the substitution of certain project components by other, cheaper solutions.

##### **3.2.3 Implementation Time**

Average implementation time was 3.3 years outturn against 3.1 years forecast. The length of the implementation period reflects the fact that the projects were large scale, often composite schemes with phased installation, and thus many entered the operational phase in stages.

Four projects were significantly delayed (i.e. by more than 6 months); for 3 of these, implementation was deliberately slowed down because market demand developed less favourably than expected. The fourth encountered start-up problems with new technology. It is illustrative of the generally high quality of implementation that only one single project was delayed for technical reasons.

In general terms, project implementation was well-managed and where modifications to initial plans were required in the interest of the project, such modifications were normally stringently controlled.

### **3.3 Operational performance**

#### **3.3.1 Technical**

Two projects were deficient in this respect because they suffered an unexpectedly early technological obsolescence, and countermeasures were not taken soon enough: both projects eventually failed. They were characterised by ambitious industrial innovation and demonstrate the substantial risk attached to such projects. This raises a question mark over the soundness of financing innovative projects of this type with loans on quasi-market terms.

Of the remaining 13 projects, 11 were further developed and expanded over the years after implementation completion. Six were significantly enlarged in terms of production capacity, and 5 were modified to allow for further development and upgrading of the final products (typically, such modifications also resulted in some capacity increase). In 4 cases, proper technical operation of the projects was ensured only thanks to initial significant increases in investment cost.

#### **3.3.2 Commercial and marketing**

For 10 projects, market demand developed less favourably in the early operating years than forecast. This is not surprising given that all projects entered production during the late 1980s or early 1990s, at a time when European economies were hit by a severe recession.

Four projects failed commercially. In 3 cases, the projects were unable to provide an adequate response to the unexpected changes in market conditions; 2 were subsequently dismantled, the third partly survived thanks to a complete company restructuring. The fourth project was, from the outset, over-sized as a result of the promoter's optimistic market forecasts, and was never utilised economically.

Of the remaining 11 projects, 2 suffered from the general demand slow-down but weathered the storm and are now in a position to benefit from a likely future improvement in commercial conditions.

Finally, 9 projects can be considered commercially successful, in most cases because, although hit by the general recession, they showed flexibility in adapting to take advantage of those areas of the market with the best prospects.

In the overall assessment of commercial performance, marketing strategy and management emerged as the decisive factors. Projects' physical elements rarely determined success or failure. The successful operations were those where management demonstrated the ability and competence to forecast market developments, envisage profitable solutions and adapt initial design to market needs.

#### **3.3.3 Financial**

Due mainly to the way in which projects were defined, it was not feasible to recalculate the rate of return on investments. In 9 cases, the project consisted of components of a wider, corporate investment plan. For the remainder, the project had been gradually absorbed into the corporate complex. At the evaluation stage, therefore, the project components could no longer be separated, making it impossible to relate benefits to costs.

Nonetheless, an attempt to estimate profitability was made on the basis of available, mainly corporate, data: project cost, production and capacity utilisation, operating cost developments, output and sales figures, and prices.

Not surprisingly, commercial and financial success were closely linked. Thus, the 4 commercial failures, referred to in sec. 3.3.2, were also financial failures. Three projects were on the financial borderline, including 2 that were commercially doubtful. In 8 instances, the financial performance was satisfactory.

Thus, 7 cases (47%) were underperforming, including 4 that must be considered irredeemable. This is in contrast with the findings presented in sec. 2.3, where, at the ICR stage, only 6 of 76 projects (8%) were estimated to be financially deficient. For P15, only 2 of the 4 failures in the sample were detected as such at the ICR stage. Although the present sample of 15 projects cannot be assumed to be statistically representative, it is likely that on average, projects turn out less successful than reported in the ICRs: various negative factors, not necessarily visible at that stage, may often take some time to surface.

### 3.4 Project Impact and Relevance

#### 3.4.1 Regional Development

A quantification of project impact on regional development has not been attempted. In fact, the effects of individual investments on macroeconomics will usually be virtually impossible to ascertain.

EIB's policy is based on the assumption that a profitable project located in a less advanced region, can be safely assumed to have a positive impact on the economic development of its region. Ideally, the measure of profitability should take socio-economic benefits into consideration, but this is rarely (if ever) done in the EIB: financial profitability (*ex-ante*) was therefore, under the given circumstances, considered the best approximation available.

On that basis, one may conclude (ref. findings in 3.3.3. above) that in P15, 8 operations were likely to have had a positive impact, 3 may have had a marginally positive effect, and the remaining 4 had a negative impact.

To attempt a verification of these assumptions, EV introduced relevance indicators (Annex 3).

Applying these indicators to the present sample, it appeared that out of the 11 above-mentioned projects assumed to have a positive impact, this was confirmed for 7 while the outcome in the other 4 cases remained unclear.

These findings should be interpreted with circumspection: the methodology pertaining to the relevance indicators needs to be tested on a larger sample before it can become part of EIB's selection tool box. Moreover, it was applied at the evaluation stage only: to be effective, it should be incorporated into *ex-ante* appraisals so that intentions and objectives can be properly compared with actual results. Nevertheless, the approach could be useful in detecting cases where the EIB has a clear value added in terms of the contribution of operations to its statutory objectives.

#### 3.4.2 Employment

While at appraisal the projects were presented as having a mildly negative overall impact on direct employment creation, by the evaluation stage substantially more jobs had been eliminated than created, a result reflecting the 1990s drive towards higher labour productivity especially in large manufacturing industries. The present study, however, does not cover the induced effects in other sectors of the economy, which are likely to be far more important. In terms of employment impact, the ICRs seemed particularly optimistic.

The quality of the employment offered by these industries should also be taken into consideration. In most of the projects involving extension and modernisation, employee skills increased markedly, and the 2 green field operations recruited a significant proportion of highly skilled workers. "It is increasingly acknowledged that the competitiveness of regions is dependent on the know-how and skill of their people"<sup>10</sup>. An area that boasts a qualified workforce tends to attract other industries requiring a similar level of skills; this in turn leads to improvements in remuneration and buying power with important spillover effects on the local economy.

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<sup>10</sup> European Commission : "First Cohesion Report", Brussels, 1996.

### 3.4.3 Other Objectives

Six projects were eligible for EIB support under criteria other than regional development: 1 was expected to improve the environment and 5 to raise European industrial competitiveness.

The environmental project was a notable success, not least thanks to the monitoring efforts deployed by the EIB. Regular contacts during implementation helped ensure that the project was brought into line with applicable regulations more quickly than would otherwise have been the case.

Two of the 5 projects supporting European competitiveness were equally successful but the remaining 3, all principally aimed at the introduction of advanced technology, ended in failure.

## 3.5 EIB's Contribution

### 3.5.1 Loans

On average, projects were financed 57% by own funds, 33% by EIB loans and 10% by other external loans against a planned breakdown of 52%, 36% and 12% respectively. The predominance of own funds is an indication of the generally robust financial position of EIB's borrowers.

Eight projects were, in accordance with original plans, financed without or with only marginal support from external sources other than the EIB. Of the remaining 7 cases, where modifications to project design and hence project cost occurred, finance plans were altered: 4 needed additional external finance (non-EIB); the remaining 3 relied entirely on own resources.

In 14 out of 15 cases, project implementation commenced before EIB's formal appraisal. However, in virtually all cases, unofficial proceedings between the promoter and the Bank had begun some time before this.

Loan maturity varied considerably: the shortest maturity granted was 4 years (one case) while the longest was 14 years (two cases). Clients' requirements in this regard tend to be determined by corporate cash flow, and the EIB tries to be flexible in accommodating their wishes, provided these seem financially reasonable and to the extent that such funds are available. The sample confirmed this.

Two out of 15 loans were repaid early. All other loans were serviced regularly, 9 until final maturity, 4 still outstanding.

A notable feature of EIB's involvement in industry financing is its restriction to a single product: loans. Although this study contained few projects eligible under the objective of raising the technological competitiveness of European industry, even this limited sample clearly points toward the need for providing access to seed capital upstream of traditional venture capital financing. High technology has been shown to entail unusually high risks, particularly in areas like research and development: the EIB's lending practices will have to be adapted if it envisages including such projects in its industrial portfolio.

### 3.5.2 Appraisal and Monitoring

The timing of involvement in the projects meant that the EIB was not in a position to significantly influence the design of the projects. The quality of the latter and the management competence of most promoters suggest that closer monitoring procedures may be of limited usefulness. Only exceptionally was the technical implementation followed closely by the Bank: in one case the Bank's follow-up included close monitoring of specific environmental conditions, and by that means the final technical project outcome was substantially improved. In one other case, monitoring procedures played a decisive role: EIB's refusal to renegotiate loan conditions at a delicate pass forced a project promoter in serious financial difficulties to accept a complete company restructuring. This included the entrance of a new majority shareholder, assuring the survival of the company and hence of the project.

In general, however, EIB's monitoring procedures were mainly directed towards tracking credit risk rather than project performance. In some cases, therefore, project development and performance were followed by the EIB on an irregular basis during implementation and rarely if ever during operation. One failure remained undetected and one lending opportunity, according to the promoter, was missed. The EIB does not impose regular reporting on its promoters. Some of them complained about a lack of focus on client needs.

### **3.5.3 Client Opinions**

Most clients stated that they had opted for EIB financing principally because of the competitiveness of the corresponding loan conditions. Some were particularly attracted by the availability of longer maturities, and a few mentioned advantages connected with the "seal of approval": the fact that they had been selected by the EIB facilitated access to complementary finance. Although projects would undoubtedly have been carried out even if Bank loans had not been obtained, promoters generally agreed that EIB's competitive financing conditions were an important element in the successful realisation of their projects.

### **3.5.4 Industrial Strategy**

If the EIB is to make a significant contribution to industry in Europe, it should develop a strategy to achieve this goal, clearly defining its complementary role to commercial financing. It could, for instance, aim at smaller industries with less ready access to international capital markets. It should also seek to improve client satisfaction rather than pursue a policy dominated by lending targets. A proper mix between infrastructure and industrial lending, particularly to those industries with high employment effects, might also be examined to maximise development effectiveness. These changes are likely to be imposed upon the EIB as a result of growing competition on the capital markets and the need to show complementarity with commercial financing.

## INDIVIDUAL PROJECT EVALUATION - FIELD VISIT

### Model Questionnaire

The objective of the visit is to learn how the Project has performed up to now and since the EIB last reviewed it in terms of capacity, production, productivity, quality control etc., and how it has influenced the development of the promoting company with regard to marketing/sales and profit generation. Furthermore we want to understand what effects the Project may have had on its surroundings, notably environmental impacts and economic/social development in the region.

Compare with initial plans/forecasts and evaluate recent developments in the light of their effects on project operations for the following items where appropriate.

1. PROJECT PROMOTER
  - 1.1 identity, legal and statutory framework
  - 1.2 shareholdings and group relations
  - 1.3 organisation and structure; business activities
  - 1.4 financials, accounts
  - 1.5 management
  
2. COMMERCIAL ASPECTS
  - 2.1 market demand - competition - market supply
  - 2.2 marketing and distribution
  - 2.3 sales and prices
  
3. TECHNICAL / PHYSICAL ASPECTS
  - 3.1 physical components of project, technology, capacity
  - 3.2 implementation; timetable
  - 3.3 production
  - 3.4 raw materials, energy input
  
4. PROFITABILITY AND FINANCIAL
  - 4.1 investment cost and rate of return
  - 4.2 impact on corporate accounts
  - 4.3 financing of project, EIB loan
  
5. ENVIRONMENT
  - 5.1 polluting effects and protective measures
  - 5.2 conformity with legislation (national and EU)
  
6. ECONOMIC AND COMMUNITY OBJECTIVES
  - 6.1 eligibility and economic objectives
  - 6.2 employment
  
7. CONCLUSIONS
  - 7.1 How successful is the project with respect to ensuring a sustained performance?
  - 7.2 Has EIB (through internal procedures; lending approach) influenced the course of the project or promoter?



<b>SAMPLE OVERVIEW</b>					
<b>N.</b>	<b>Sector</b>	<b>Purpose and Project Type</b>	<b>Project cost, m ECU</b>	<b>EIB loan, m ECU</b>	<b>Implem. time, years</b>
1	Oil refining	Productivity increase; pollution abatement; conversion of production to higher grade and better quality products. No overall capacity increase.	439	196	6.1
2	Chemicals	Productivity and capacity increase; product quality improvement.	42	23	1.5
3	Transport equipment	Productivity increase; introduction of new products replacing older ones. No overall capacity increase.	148	18	3.1
4	Electrical engineering and electronics	"Greenfield" project; new production capacity.	69	11	2.0
5	Glass production	Productivity increase and shift in capacity from one product type to another; no overall capacity increase.	68	20	1.1
6	Paper production	Productivity and capacity increase; improvement of product quality.	143	30	1.6
7	Standardised factory buildings	Mainly "greenfield" project; productivity increase and creation of new capacity.	22	12	4.1
8	Paper production	Productivity and capacity increase; improvement of product quality.	127	52	2.8
9	Electrical engineering and electronics	Product development and capacity increase.	66	7	4.1
10	Wood products	"Greenfield" project; new production capacity.	66	18	3.0
11	Transport equipment	Productivity increase; development of new products replacing older ones. No overall capacity increase.	76	36	3.6
12	Glass production	Capacity increase and up-grading of existing product range.	115	48	3.5
13	Food processing	Productivity and capacity increase.	77	33	5.4
14	Construction materials	"Green field" project; new production capacity.	109	6	2.8
15	Electrical engineering and electronics	Productivity and capacity increase; product development and quality improvement.	144	50	4.1

Cost, loan and implementation time data relate to project outturn.

**DRAFT****REGIONAL DEVELOPMENT****Relevance Indicators for Industrial Projects**

The following list includes items to be examined at appraisal. Impact can be expected to depend on the number of indicators confirmed as relevant for a given project, and on the degree of quantification of the selected indicators.

Impact expectations as recorded at appraisal should be verified *ex-post*, at implementation completion and/or for a possible evaluation.

1	Project profitability <ul style="list-style-type: none"> <li>▪ rate of return on the investment</li> <li>▪ effect on promoter's overall financial situation</li> </ul>
2	Extent to which financial benefits of project stay in region or are transferred outside region
3	Employment <ul style="list-style-type: none"> <li>▪ safeguarded</li> <li>▪ increased</li> </ul>
4	Increase in employment skills required
5	Use of regionally produced raw materials, primary products etc. <ul style="list-style-type: none"> <li>▪ safeguarded</li> <li>▪ increased</li> </ul>
6	Use of regional sub-contractors etc. <ul style="list-style-type: none"> <li>▪ safeguarded</li> <li>▪ increased</li> </ul>
7	Other spin-off effects, e.g. establishment (or closure) of related enterprises etc.
8	Technology / know-how transfer benefiting region
9	Improvements in supply of goods and services in region
10	Improved housing, living and social conditions
11	Improved infrastructures
12	Increased attractiveness of region

## **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, French, German, Italian and Portuguese).

These reports are available from:

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