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Synthesis Report

Evaluation of Lending in New Member States prior to Accession

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EVALUATION REPORT

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NOTICE

The EIB has an obligation of confidentiality to the owners and operators of the projects referred to in this report. Neither the EIB nor the consultants employed on these studies will disclose to a third party any information that might result in a breach of that obligation, and the EIB and the consultants will neither assume any obligation to disclose any further information nor seek consent from relevant sources to do so.

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GLOSSARY OF TERMS AND ABBREVIATIONS

Absorption capacity	The ability to use approved funds in the timescale and manner envisaged
ACP	African, Caribbean and Pacific (countries)
Acquis-communautaire	The total body of EU law
Borrower	The legal persona with whom the Bank signs a Loan Agreement.
bp	basis points (one hundredth of one percent interest)
CA	EIB's Board (q.v.) The EIB Board of Directors, which has sole power to take decisions in respect of loans, guarantees and borrowings.
CD	EIB's Management Committee (q.v.)
CEE	Central and Eastern Europe
COP	Corporate Operational Plan
EBRD	European Bank for Reconstruction and Development
ECOFIN	EU Economic and Financial Affairs Council
EIA	Environmental Impact Assessment
EIB	European Investment Bank
EIRR	Economic Internal Rate of Return
EU	European Union
EU10	Countries joining the EU on 1 May 2004
EU12	EU10 plus Bulgaria and Romania
EV	EIB Operations Evaluation (Ex-Post)
FIRR	Financial Internal Rate of Return
FVA	Financial Value Added
FYR	Former Yugoslav Republic
GDP	Gross Domestic Product
GED	Gestion Ēlectronique Documents (Electronic Documents and Records Management System)
ISPA	EU grant instrument (Instrument for Structural Policies for Pre-Accession)
	Management Committee Internal EIB committee, comprising the Bank's President and Vice-Presidents
NMS	New Member States (EU12)
Ops-A	EIB Directorate for Lending Operations – EU Members, Acceding, Accession and Candidate States
OCT	Overseas Countries and Territories
PCR	Project completion report
PHARE	EU grant instrument (Poland and Hungary: Assistance for Restructuring their Economies)
PJ	EIB ProJects Directorate – Responsible for ex-ante project techno-economic analyses, the preparation of the Technical Description, and the physical monitoring of implementation and completion.
PPP	Public Private Partnership
Project	A clearly defined investment, typically in physical assets, e.g. a specific section of road, a bridge, etc.
Project Pipeline	Those projects which have been signalled to the Bank, but have either not yet been approved by the Management Committee, or have been approved but not yet signed. These include projects under active appraisal and those in the process of contract negotiation prior to signature.
Promoter	Normally the persona responsible for identifying and developing a project. The promoter may also be responsible for operating and/or implementing the project.
RM	EIB Risk Management Directorate, responsible for credit appraisal and portfolio management
RSFF	Joint EIB/Commission Risk Sharing Finance Facility
SAPARD	Special Accession Programme for Agriculture and Rural Development
SEE	South Eastern Europe
SFF	EIB Structured Finance Facility
SME	Small or medium sized Enterprise. A company with less than 250 employees.
SPV	Special Purpose Vehicle – A company, with its own legal persona, set up for a limited set of specific purposes, e.g. to borrow for the construction of a project.
TA	Technical Assistance
Technical-description	Project definition - the basis of the Loan Agreement; prepared by PJ.
VA	Value Added

EXECUTIVE SUMMARY

Introduction

This evaluation concentrates on EIB lending in the twelve new member states (NMS), prior to their accession to the EU, under the various Central and Eastern-European (CEE) mandates and pre-accession facilities which were put in place by the Council and the Bank to allow for financing of projects during the pre-accession period.

This evaluation report has considered a total of 78 projects, representing 23% of all projects signed during the entire pre-accession period in the 12 new member states. Of these, 31 have been evaluated in depth (18 during previous evaluations and 13 during this evaluation).

Alignment of EU and EIB Priorities

In general the Bank has matched signature volumes closely with the relevant mandate ceilings. Disbursements follow signatures for EU12 during the first half of the period, after which an increasing gap begins to appear. Despite recent action taken by the Bank, some EUR 6.3bn of loans signed during the pre-accession period currently[1] remain to be disbursed (18% of the total amount signed).

There appears to be a clear trend of increasing Bank lending per capita with increasing GDP per capita. Whilst it is also true that the absorption capacity of a country is likely to be positively related to its GDP, nevertheless, this finding might be considered as a somewhat counter intuitive one given that the Bank's intervention in these countries had a strong regional development component.

EU support to eastern Europe aimed at assisting in the transition of these countries to stable democracies with functioning market economies and preparing those economies for EU entry. Early EIB operations were of a pioneering nature and the need was so great that activity of almost any kind was beneficial.

With the Council declarations in 1993 and 1994, the focus of EU and country involvement began to move towards a more focussed agenda aimed at achieving the Copenhagen criteria[2] and the ultimate accession of the EU10 countries to the Union. Whilst much of the initial effort was directed towards the development of institutional and legal frameworks, the process of adoption of the *acquis communautaire* also highlighted those sectors which were in need of priority investment and, through the development of detailed Partnership Agreements, the EU and individual candidate states developed joint priorities for investment at individual country level.

Declaring itself to be fully supportive of EU policies and priorities in the region, the Bank's approach was to reserve for itself a wide mandate for intervention as illustrated when setting the first pre-accession facility in 1998:

"The facility, as well as the lending mandate, shall be used in order to facilitate and accelerate progress in all sectors normally eligible for EIB financing, notably in areas of key European Union policy objectives."

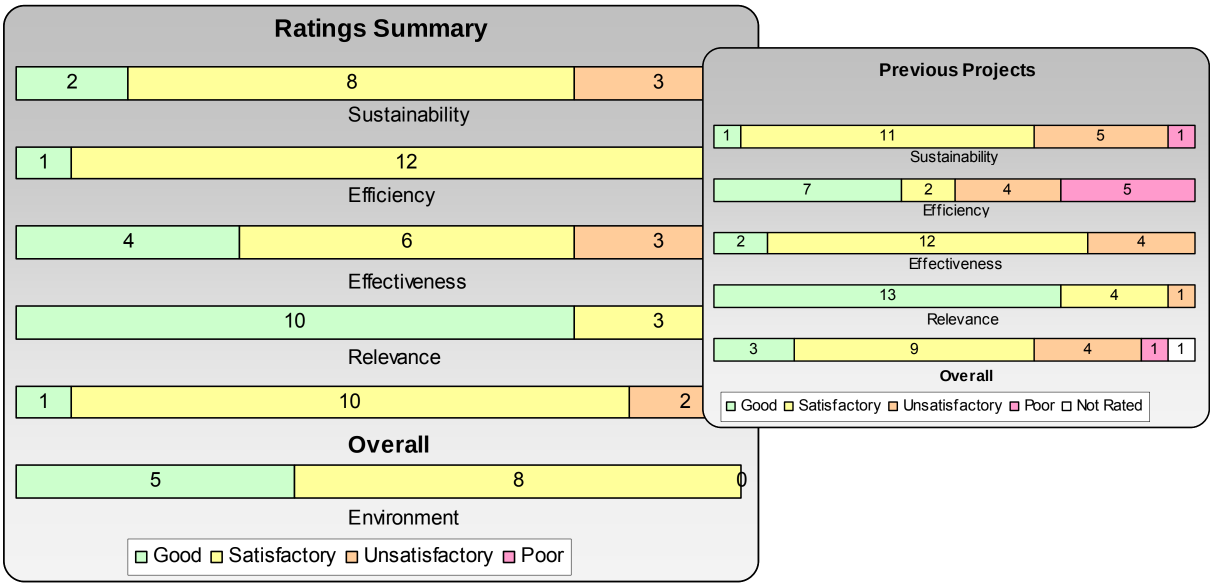
However, key operational constraints limited the activities of the Bank in the region: budgetary constraints (linked to the Maastricht criteria), limited supply of bankable projects (linked to the absence of complimentary sources of funds), and increased lead time for project development (linked in some cases to the application for EU grant finance). The result was that in the process of putting into effect the same policies and priorities, the Bank recognised that the outcome would be more determined by practical operational constraints.

Project performance

Individual operations were evaluated on the basis of internationally accepted evaluation criteria of Relevance, Efficacy, Efficiency and Sustainability (see graph below). The individual ratings are considered together to produce an overall rating for the project. This is not an arithmetical exercise, and reflects the extent to which individual aspects contribute to the whole on a case by case basis. Environment is rated separately, but is already accounted for within the four main ratings.

[1] As at 01.09.08

[2] See Appendix 1



The overall ratings confirm that the majority of projects which the Bank financed in pre-accession countries performed well under difficult operating conditions. Relative deficiencies were linked to cost overruns and delays which were not anticipated and the inability to tackle particular sectoral problems.

Projects examined as part of the current evaluation have also tended to perform better than those older projects evaluated as part of earlier themed evaluations (see ‘Previous Projects’ box above). This is particularly marked for the Efficiency rating, and is probably indicative of a general improvement in project identification and selection as a result of increasing experience of working in the region.

EIB contribution and project-cycle management

For the majority of projects examined, IFI support was the only available source of long term funding. The Bank’s financial contribution was therefore high, giving the Bank considerable potential influence over the projects. In most cases these projects were also part of a series of investments in a well defined programme, some of which also benefited from EU grant finance. This combination of circumstances gave the Bank considerable leverage not only over the project but also over the sector.

The main contribution of the Bank to other aspects of the project tended to be through the enforcement of the Bank’s policies on procurement and the environment which, in most of the cases examined, required a considerable staff resource input. In many cases the Bank also insisted on the appointment of experienced international consultants to assist the promoter in implementing the project.

These contributions were mainly made at project level and where occasionally a suggestion was made at appraisal for the introduction of a conditionality extending beyond the project, this was either not followed through or diluted. As a result, the outcome of a project was sometimes affected by sectoral issues which the Bank did not directly address. In certain sectors (water for example), there was close policy alignment between the Bank and the Commission, allowing a larger sectoral view.

EIB project cycle management has been developed over a long period of time and is systematic, structured and well adapted to the vast majority of the Bank’s operations. In the majority of cases projects were well handled from a procedural point of view, and 10 out of the 13 projects examined were rated satisfactory or better. Through the permanence and the quality of its relations with local authorities, the EIB supported improvements in project preparation. Of the three projects which were considered unsatisfactory, it was felt that although sector difficulties were correctly identified, insufficient allowance was made for these within the subsequent Bank operation. In addition, a number of individual issues were highlighted which could assist in the management of future projects in transition economies.

Preparation for Accession

The extent to which the Bank had contributed to assisting beneficiary countries with their pre-accession objectives was identified as a key issue. Some 30 further projects were therefore selected for extended scope analysis with the aim of providing a broader view of issue than can be provided by the smaller in depth sample of projects.

The following indicators were used as the basis for assessing the Bank's contribution to the accession process.

> *Supporting Sector Improvement Towards EU Standards* - The projects which the Bank has supported undoubtedly made a positive contribution to the accession process, and in some cases the Bank worked hard to overcome wider operational constraints, but the impression is left that even better results could be obtained by concentrating more effort at country and sector level.
>
> *Supporting the Development of Financial Markets and Products* - The availability of disbursements in local currencies made a positive, if relatively small, contribution to the accession process. The Bank was also active in trying to unlock public borrowing constraints through the use of PPP project structures, although these efforts were perhaps less successful.
>
> *Support for the Implementation of EU Directives* - The conditions of disbursement enforced by the Bank illustrate the importance attached to technical assistance, Project Implementation Units, environmental expertise, environmental approvals and permits, and international tendering.
>
> *Cooperation with the Commission and IFIs* – Approximately one third of projects examined were co-financed with the EU. When compared with levels of co-financing within the EU, this could be considered as a relatively high level. However, given common priorities, lower lending volumes and the more limited project pipeline opportunities during the pre-accession period there would appear to be scope to have improved cooperation. The extent to which cooperation took place at country and sector level is more difficult to establish independently as this is not recorded in project files. There are indications that cooperation in the water sector in particular was more developed than in other sectors.

At a project level the Bank's operations had a positive impact on the accession process but at a sector and country level, the Bank's positive impact was limited by a number of operational and practical constraints. Given that in most cases the attractiveness of the Bank's funds gave it significant influence during the pre-accession process, it could be argued that the Bank should have done more to develop sectors and institutions which would in the longer term have increased the pipeline of bankable projects and allowed it to further improve the alignment of its activities with EU priorities.

TABLE OF RECOMMENDATIONS

	EV Strategic Observation & Recommendation	Response of the Operational Departments
1	**Observation:** The Bank acknowledges that its operations in pre-accession countries were subject to a number of operational constraints (§3.4). The effect of these constraints has been: · To relatively prioritize more developed economies (§2.3) · To prioritize less difficult projects and sectors which are not necessarily well aligned with EU accession priorities(§2.3 and §6.1) · In one case, by multiple successive operations, to exceed the capacity of the country and its sectors to absorb approved loans (§6.2) EV acknowledges the efforts made at the time to proactively intervene in local currency markets and to overcome obstacles to the funding of small projects by municipalities, as well as more recent efforts to provide institutional support to tackle the identified disbursement gap. **Recommendation:** The Bank should increase its efforts to overcome operational constraints which limit the impact of its policies in accession countries. *In the first instance, it is recommended that an inter-directorate working party should be set up to review all aspects of the Bank's intervention in the accession process with a view to recommending practical measures targeting future 'log jams'.* These renewed efforts should involve: · The adjustment of performance indicators to incentivise problem solving behaviour on a multi-disciplinary basis. · The introduction of strong and transparent country and sector aspects to lending policy (already partly achieved through Operational Guidelines and Sector policies) but moving from a passive knowledge of the problems to targeted actions designed to overcome them. · The availability of adequate TA resources in support of operational staff. · The regular review of the lending portfolio on a country and sector basis as a tool to monitor progress, target constraints and adjust lending policy.	The 'bankability' of countries and their projects increases with development level. It is not surprising that lending in these countries should reflect this fact. A project can be aligned with EU accession priorities without necessarily being co-financed with EU grants. EU subsidies are a first level of support for the weakest regions. EIB concentrates on investments that are already bankable. In fact, the degree of coordination with the EC DG REGIO on ISPA projects was high in most countries, including commonly designed conditionalities, although to achieve an adequate lending volume the Bank had to group projects. The Bank also gave considerable technical advice to the EC on large transport and environment projects via the "contrat cadre". *Agreed. In practice, such a review needs to stay focused on project and sector level issues and establish appropriate mechanisms for engaging with the EC in a common dialogue with the countries concerned.* The ongoing revision of the Bank's value added methodology should contribute to a clearer and more transparent definition of volume and value orientated operational targets, underlying the Banks value orientated lending focus. Within the New Member States, JASPERS is now active with some 55 full time staff in supporting project preparation.
	Additional comments from Operational Departments: New initiatives In the Western Balkans and for quite some time now, the Bank, other IFIs and the EC participate to joint meetings and fora covering specific sectors at regional level. These form the basis for identification of priority investment projects, which in turn can be supported by IPA grants in the context of the Infrastructure Projects Facility launched by the European Commission in December 2007 with the involvement of EIB, EBRD and CEB. The EC and the three partner IFIs are now working on setting up a Western Balkans Infrastructure Initiative aiming at meeting the needs and priorities of the beneficiary countries (ownership) by pooling grant resources for technical assistance and co-financing between grants and loans, while increasing coordination between European financiers and donors. This initiative is a first step towards a wider Western Balkans Investment Framework to be put in place by 2010 and was endorsed by the European Council in June 2008. The Bank has stepped up TA activity significantly in the Western Balkans to overcome weaknesses in preparation and implementation of EIB projects and additional staff and funding resources have been approved from 2009. The Bank's technical services collaborate closely with DG ELARG to ensure the quality of other TA instruments managed by the Commission and transfer sector knowledge from previous experiences. In Turkey, similar initiatives based on increased cooperation between the EC, the EIB and in the future also the EBRD aim at optimizing the EU grant / EIB funding mix for priority projects.	

	EV Strategic Observation & Recommendation	Response of the Operational Departments
2	**Observation:** Given that the economies of the countries in the region were in transition, and that several of the promoters were acknowledged to be inexperienced, insufficient allowance was made at approval stage for possible cost and time over runs (§4.1.1). This was despite the fact that the risks were clearly identified in appraisal documentation. **Recommendation:** The appraisal should present a realistic estimate for implementation (as likely to be low as high), or present a range of possible outcomes which take account of the identified risk factors.	Agreed. Delayed implementation, particularly in Romania and Bulgaria has been a major problem for EIB but even more so for EC due to N+2 rules. However, the pressure to approve immature projects comes from promoters who need to secure financing before completing their detailed studies and from the EC needing to commit available grant funds. The services will continue to refine the realism of implementation schedules in the light of country experiences.
3	**Observation:** Having identified the project risks at appraisal, these were not always followed through to project implementation (§6.2). **Recommendation:** Risk factors which are identified at appraisal should be accompanied by mitigation proposals. These in turn should be turned into enforceable contract conditions which are then actually enforced.	Agreed. Part of the new monitoring and learning coordination function will include internal training for staff on the design of loan conditions.
4	**Observation:** Whilst all projects demonstrated an acceptable economic rate of return ex post, there did not appear to be a consistent or transparent approach to the assessment of economic return at appraisal for different sectors and countries(§4.2.1). The approval of project 2 was on the basis that intangible environmental benefits arising from the transfer of travelers from more polluting modes of travel would increase the calculated rate of return. This argument is one which the Bank should now seek to put on a more secure evidential basis (§4.2.2). **Recommendation:** The Bank should adopt a more transparent approach to the benchmarking of rates of return for different sectors and countries and review the current state of research into the intangible environmental benefits of public transport projects with a view to quantifying the importance of their contribution.	Operational constraints and the nature of projects mean that it is frequently not possible or even relevant to calculate an ERR. Nonetheless, the scope for introducing more transparent criteria between sectors is being addressed as part of the present update to the VA methodology. The Bank is aware of the latest methodologies to assess environmental externalities, but a pragmatic use of resources means that the appraisal effort ceases once the Bank is satisfied that the project will pass the threshold. An up-date report on appraisal methodologies is to be issued in the near future.
5	**Observation:** The evaluation found shortcomings in the recording of data relating to the mandates of operations, together with an absence of information on co-funding (§2.2 and §7.2.1). **Recommendation:** The capture of data via the Bank's Serapis application is now a complex and specialised task involving continual updating of project information. The regime of quality and integrity checks should be strengthened, and information on co-funding should be systematically recorded.	Agreed. As part of proposals to restructure the organisation and responsibilities for physical monitoring the services will make recommendations relating to quality control of electronic project data. Operational guidelines will be updated to ensure that Serapis information on co-funding will be formally updated at key stages in the project cycle, including appraisal, signature and PCR.

	EV Strategic Observation & Recommendation	Response of the Operational Departments
6	**Observation:** The project relating to flood relief had a number of unusual aspects (§3.5.1). At the time there was no obvious established eligibility for the operation. This has now changed, but such projects still presents particular challenges. No particular conditionalities were imposed to help prevent a similar event. **Recommendation:** The modalities of reconstruction and restoration projects following natural disasters should include risk mitigation aspects. These in some instances will not be directly linked to the infrastructure.	Similar, more recent, projects have included provision for flood prevention works. Agreed. The operational guidelines will be updated to specifically deal with risk mitigation.
7	**Observation:** The process of institutional learning and handover must be formalised to a greater extent than at present where changes in personnel may have contributed to a lack of awareness of cumulative problems over several operations (§6.2). The Bank's (monitoring) input was significantly affected by a high turnover of staff and a lack of formal handover procedures (§6.4). **Recommendation:** Key project data and post approval decisions should be contained in an easily accessible, cross directorate, summary document which is updated on a regular basis, and a formal handover procedure should be established.	The services will make proposals to restructure the organisation and responsibilities for physical monitoring to improve learning and continuity in the near future. In principle, all key project data and post approval decisions should be recorded in Serapis. Agreed. Establishing a common monitoring summary document between directorates would improve continuity, audit trails and knowledge management.

1. INTRODUCTION

This evaluation is being undertaken following the recent update of the Operations Evaluation (EV) Strategy and the subsequent revision of the EV Programme for 2008. The evaluation concentrates on EIB lending in the twelve new member states (NMS)[3] prior to their accession to the EU, under the various Central and Eastern-European (CEE) mandates and pre-accession facilities which were put in place by the Council and the Bank to allow for financing of projects during the pre-accession period.

The focus of the evaluation is on the relevance and performance of the projects, as well as EIB's contribution and performance in these projects. Whilst all of the Bank's priorities are considered, a particular assessment was made of the extent to which the Bank, through its operations in the twelve NMS, assisted them in preparing for accession to the EU.

The evaluation has two primary functions. Firstly, to increase transparency to the EIB's governing bodies and external stakeholders and, secondly, as a learning exercise to provide assistance to the Bank's operational departments, thereby increasing the Bank's value added in future operations.

Six instruments (four mandates and two pre-accession facilities[4]) are covered by the evaluation, although projects chosen for in depth evaluation relate to the more recent instruments. Any other regional Mandates, country-specific Protocols or individual Article 18 operations relating to the twelve NMS were not evaluated, nor are EIF operations in these countries included.

1.1 APPROACH AND METHODOLOGY

The comparison of ex-post results with the expectations and objectives at appraisal is the main basis for the evaluation of the operations. In accordance with the Bank's evaluation procedures, individual projects were rated according to four categories: "Good", "Satisfactory", "Unsatisfactory" and "Poor"[5]. The evaluation was carried out by internal EV staff with the assistance of consultants, and the relevant operational departments (OPS-A, PJ and RM) were consulted at the various stages of the evaluation.

The following steps are key elements for this evaluation:

A general review of EU, Member State and EIB policies and strategies, looking principally at the mandates and facilities governing EIB lending during the pre-accession period.

A comprehensive portfolio review - analysing EIB financing trends, sector and country distributions for 343 projects signed in the 12 new member states prior to their respective accession dates;

A review of previously evaluated projects – looking at the performance of 18 projects already evaluated as part of previous ex post evaluations. These span the whole period of pre-accession.

The in depth evaluation of 13 projects signed between 1997 and 2007 but not previously evaluated. The project sample is representative of the pre-accession financing of the Bank during the later half of the accession process. The table below summarises the main features of the selected projects, covering 7 EU Member States.

Detailed project analysis and field visits for all 13 projects have been conducted. Individual evaluations involved meetings with the organisations responsible for project implementation, operation and policy. Site visits included meetings with responsible company managers, representatives from national, local and regional authorities. Individual evaluation reports have been prepared and discussed with the operational staff associated with the project, and the main elements were provided to project promoters for their comments. The information contained in these reports is of a confidential nature and availability is restricted to EIB staff.

Extended analysis – a desk review of an additional sample of 30 further projects completed within the period 1997 to 2007 which had not previously been evaluated in depth was carried out with the purpose of examining the contribution each made to the accession process.

[3] Poland, Hungary, the Czech Republic, Slovakia, Slovenia, Estonia, Latvia, Lithuania, Cyprus and Malta, which joined the EU on 1 May 2004; and Bulgaria and Romania, which joined the EU on 1 January 2007.

[4] See Appendix 1 for details

[5] "High", "Significant", "Moderate" and "Low" for EIB contribution.

A project completion report review - based on an analysis of 62 new format Project Completion Reports (PCRs) issued by PJ during the period between 2004 and 2007.Of these, 14 were already included as part of the extended analysis above.

No.	Country	Sector	Size (EUR m)	Mandate*
1	BULGARIA	Roads	60.00	MAN
2	CZECH REP	Metro	150.00	MAN/FAC
3	CZECH REP	Water	100.00	MAN
4	HUNGARY	Power	20.00	MAN
5	HUNGARY	Infrastructure	60.00	FAC
6	POLAND	Motorways	275.00	FAC
7	POLAND	Wastewater	31.00	FAC
8	ROMANIA	Manufacturing	35.00	MAN
9	ROMANIA	Roads	225.00	MAN
10	ROMANIA	Tram	70.00	MAN
11	SLOVAK REP	Bridge	45.00	MAN
12	SLOVENIA	Motorways	160.00	MAN
13	SLOVENIA	Communications	100.00	FAC

* MAN (EU mandate), FAC (EIB facility)

This evaluation report is a synthesis of the findings of the individual evaluations and the complementary analysis, and considers a total of 78 projects for its conclusions, representing 23% of all projects signed during the entire pre-accession period in the 12 new member states. Of these, 31 have been evaluated in depth (18 during previous evaluations and 13 during this evaluation).

2. BACKGROUND

2.1 THE ORIGINS OF EIB INVOLVEMENT IN CENTRAL AND EASTERN EUROPE

Since 1963, the EIB has undertaken operations from its own resources outside the Community in support of the Community's external policies. Operations under various mandates from the Council have been guaranteed against losses either by the Member States (for example in ACP countries and OCT) or by the General Budget of the Community[6] (in all other regions outside the EU). However, prior to 1990 the Bank had not financed projects in any of the central and eastern European countries with the exception of Yugoslavia, but following the major political events in central and eastern Europe, the EU Council established a mandate for financing in Poland and Hungary, the first of a series of mandates which would later cover financing in the future pre-accession countries of central, eastern and south-eastern Europe. The Bank had financed projects in Cyprus and Malta under regional mandates and country-specific protocols, but this prior lending in Yugoslavia, Cyprus and Malta is not covered by this evaluation.

Between 1990 and end-2006, six instruments were established at various points in time to allow for EIB financing in 19 countries in the central, eastern and south-eastern European areas: four of these instruments were mandates from the Council and two were pre-accession facilities set up by the Bank in response to a request from the Council (see Appendix 1 for details).

Up to the end of 1996, the Bank provided finance in central and eastern Europe under mandate only, and these mandates were 100% guaranteed by the General Budget of the Community. The aim of the first two mandates, up to the end of 1996, was to allow the EIB to finance capital investment projects in countries undertaking fundamental economic reform. It was only after the Copenhagen Council of 1993 and the Essen Council of 1994 that the concept of "pre-accession" lending was

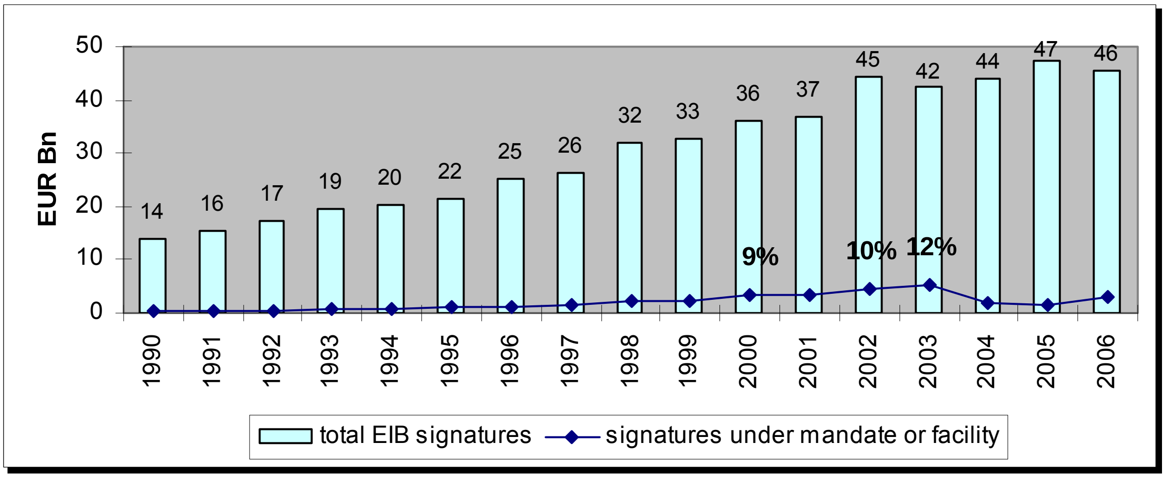
[6] In 1994, the Council established a Guarantee Fund, the financial management of which was entrusted to the Bank. The Fund was established to protect the Budget of the European Communities from risk as a result of guarantees covering loans to third countries. This Fund also covered risks related to Euratom lending and macro-financial assistance operations directly undertaken by the Commission. Modalities and procedures for payment and reimbursement between the Commission and the Bank are governed by the Implementation Agreement between the European Community and the EIB of January 1999, repealed by the Recovery Agreement between the European Community and the EIB of August 2007.

applied. The third mandate of 1997, under a 70% Community Budget Guarantee, was established by the Council on the understanding that the Bank would, in turn, set up a complimentary pre-accession facility. This first facility, authorised by the Bank's Board of Governors in 1998, was to run in tandem with the 1997 mandate.

Own resources operations under the pre-accession facility are entirely at the Bank's own risk, as they do not benefit from any Community or Member-State Guarantee. The intention was that the new pre-accession facility could be used for projects in investment-grade countries, thus allowing room under the mandates for non-investment-grade countries. Whilst lending under the facility was open to all countries authorised by the Board of Governors, projects in non-investment grade countries such as Slovakia, Lithuania, Bulgaria and Romania were still financed under mandate until these countries achieved investment-grade status.[7]

2.2 OPERATIONS UNDER MANDATE AND FACILITIES

In the sixteen-year period from 1990 to end-2006, a total of EUR 35.1bn was made available under the pre-accession mandates and facilities of which EUR 34.9bn, or over 99%, were signed. This amount represented 6.7% of total EIB signatures during this period of time. The annual breakdown of signatures under Mandate or Facility compared with total EIB signatures is shown below.



Between 1990 and 2006, the European Community also made available a total of EUR 31.7bn as grants under its three main instruments for pre-accession[8] in central and eastern Europe - PHARE, ISPA and SAPARD.

A cumulative picture of mandate and facility ceilings compared with signatures and disbursements over time is shown below. In general the Bank has matched operation volumes closely with the relevant ceilings. Disbursements follow signatures for EU12 closely during the first half of the period, after which an increasing gap begins to appear. This 'disbursement gap' of EUR 7bn in EU12 is particularly marked in some countries. Disbursements remain broadly static during the period 2004 to 2006 and this is indicative of potential absorption problems. Despite recent action taken by the Bank, some EUR 6.3bn of loans signed during the pre-accession period currently[9] remain to be disbursed.

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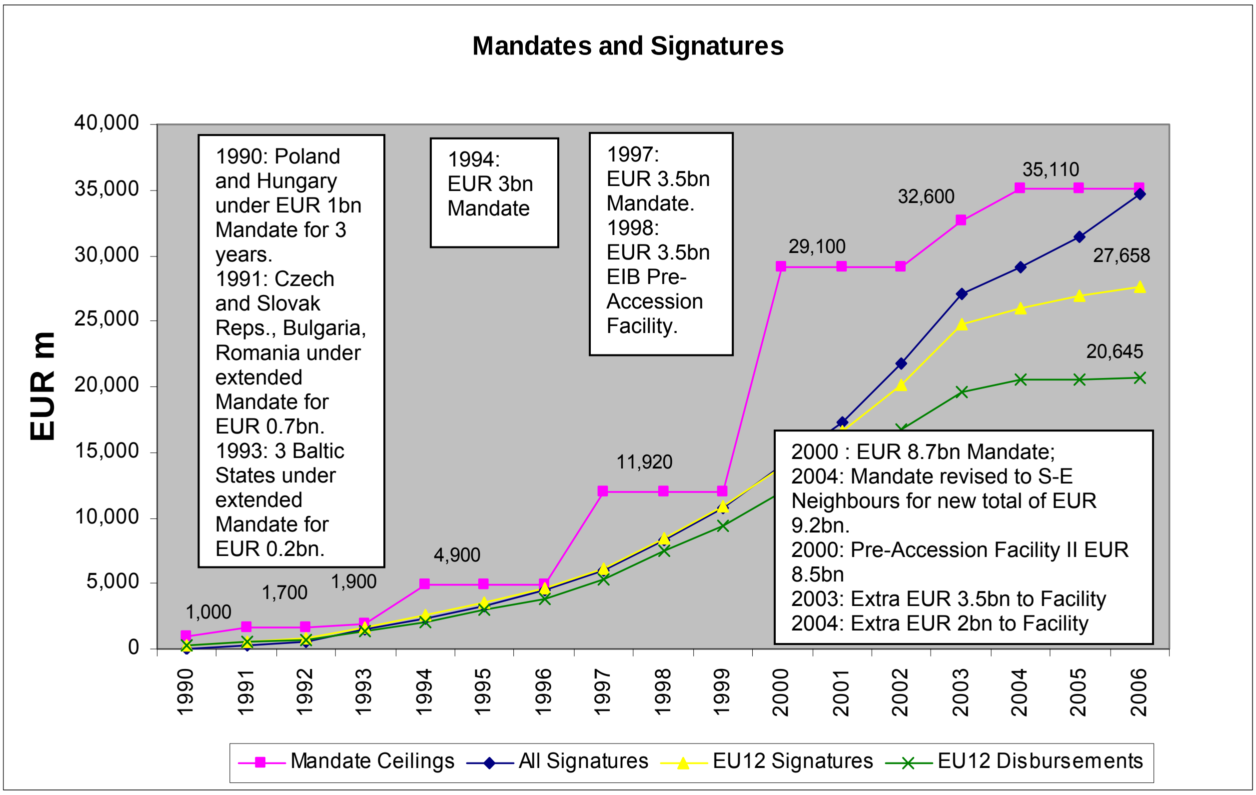
[7] Slovakia in 2001, Lithuania in 2002, Bulgaria and Romania in 2006.
[8] Included Macedonia, Bosnia-Herzegovina and Albania
[9] As at 01.09.08



Between 1990 and the end of 1997, EIB lending in central and eastern Europe was under mandate only. With the establishment of the first pre-accession facility in 1998, a comparison between signatures under Mandates and Facilities becomes possible. A steady increase is observed in signatures under Facility from the outset and they reach their highest levels in 2002 and 2003, prior to accession of ten countries in mid-2004[10]. In 2004, a general decrease is observed in signatures both under Mandate and Facility. At this point in time, the ten NMS are no longer eligible for financing under these instruments and there is a generally lower level of operations in the other countries covered by the Mandates and Facilities.

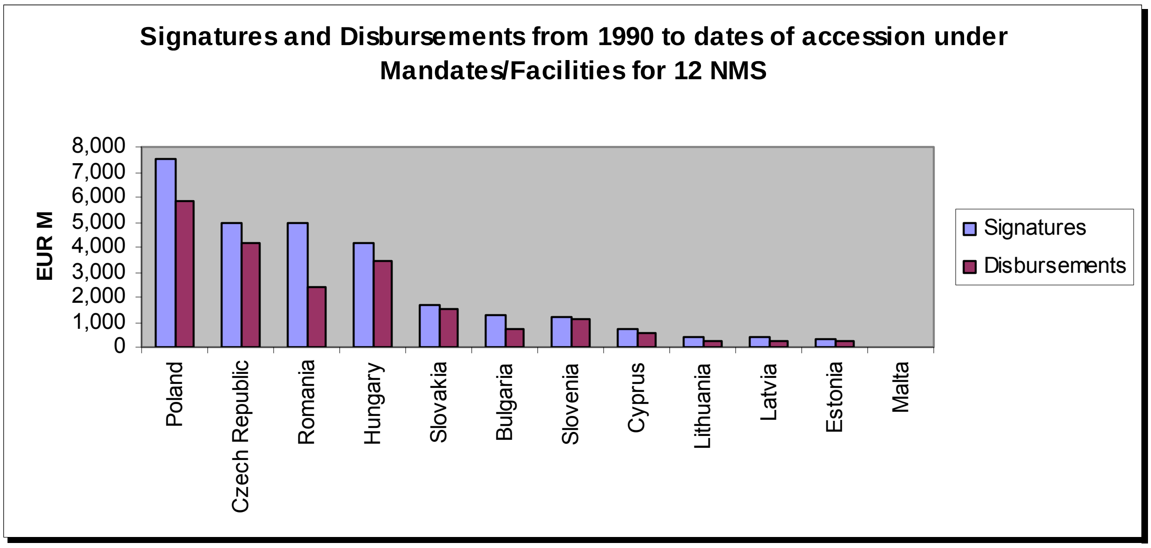
It is worthy of mention that during the examination of the Bank's databases, some EUR 1bn of operations (mostly in Romania but also in Bulgaria) were not accurately allocated to mandate/facility. Some research was required in order to allocate the relevant projects to the correct mandate. This inaccurate recording of information can lead to inaccurate reporting of EIB lending.

2.3 PORTFOLIO REVIEW

In the ten NMS which joined the EU on 1 May 2004, the Bank signed a total of EUR 21.5bn under the four mandates and two pre-Accession Facilities. In the case of Bulgaria and Romania, the Bank signed a total of EUR 6.2bn before their accession on 1 January 2007; this is a total of EUR 27.7bn in all twelve countries combined, and amounts to over 79% of the total (EUR 34.9bn) signed in all countries covered by the Mandates and Facilities[11].

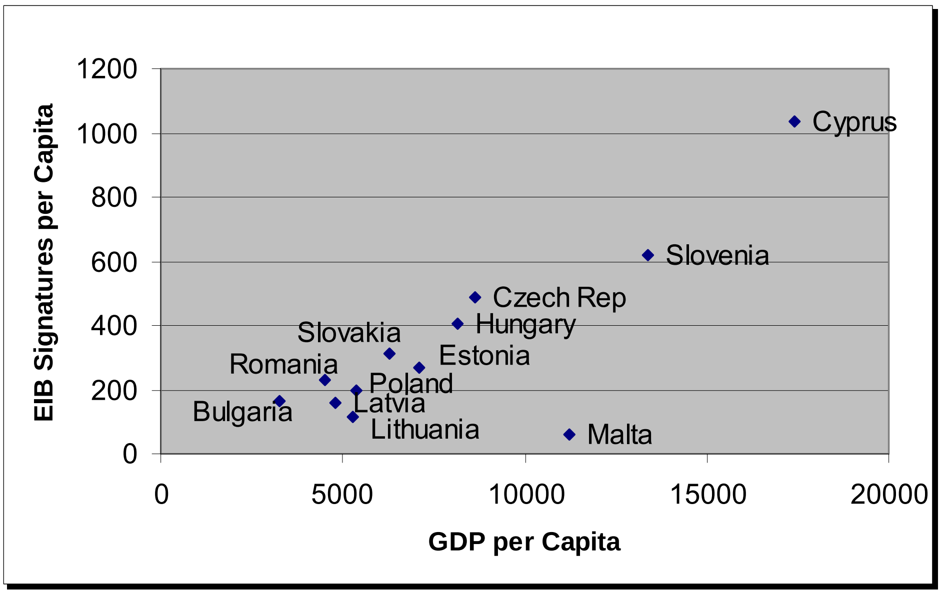
[10] See Appendix 1

[11] The remainder relating to the Balkan countries and, from 2000 – Turkey. EIB lending in Cyprus, Malta and Slovenia was also undertaken under country-specific Protocols. In Cyprus and Slovenia, this amounted to 26% and 14% respectively of lending under pre-accession mandates and facilities. In Malta, signatures under Protocols amounted to 174% of lending under the pre-accession facility.



The pattern of disbursements broadly follows that of signatures with a degree of 'overhang' beyond the accession date in all countries. This would be expected to a certain extent as loans signed during the years immediately prior to accession would not yet be fully disbursed. However, this is particularly marked in the case of Romania, and to a lesser extent in Poland, the Czech Republic and Bulgaria. The size of these 'disbursement gaps' is more indicative of problems of absorption capacity[12] than of normal implementation time lag.

It is also interesting to note that the total volumes of signatures do not follow any discernable trend in country size or degree of economic development. If population and GDP considerations are factored in, a more interesting pattern emerges, as shown in the following figure where EIB signature volumes per head of population (at accession) are compared with GDP per capita[13].

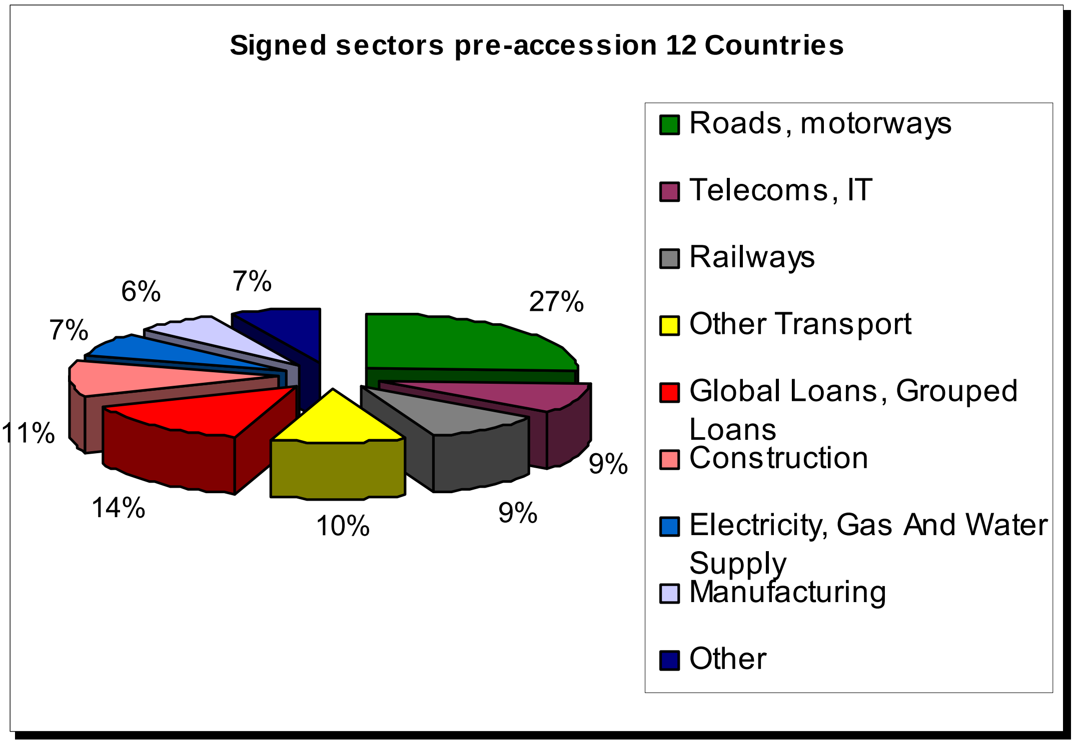


There appears to be a clear pattern of increasing Bank lending per capita with increasing GDP per capita. (As discussed above, the pre-accession mandates and facilities were not Malta's main source of EIB funds, and this explains the outlying data point.) This finding might be considered as a somewhat counter intuitive one given that the Bank's intervention in these countries has a strong regional development component, whereas the Bank seems to lend proportionally more to the more developed countries. Whilst it is acknowledged that the Bank's lending activity is also influenced by

[12] The ability of the country to make timely use of the approved funds.
[13] Eurostat figures for 2004 with the exception of Bulgaria and Romania; population 2007, GDP 2006.

the absorption capacity of the country, which is also likely to be positively linked GDP, it was not inevitable that the Bank was constrained to follow this pattern.

In the twelve countries combined, the Transport, Storage and Communication sector took the highest share of signatures up to the respective dates of accession with 55% of the total. This is followed by Global Loans at 14% and Construction at 11%. This trend is confirmed in the individual countries, with the exception of Estonia, Cyprus and Malta.



EUR 15.1bn were signed in the Transport, Storage and Communications sector in the twelve countries prior to their respective dates of accession to the EU. Almost half of the amount signed in the Transport sector, or over EUR 7bn, went to roads and motorways, representing 27% of the total. The two other big sub-sectors were Telecommunications, at 9% of the total, and Rail, also at 9%.

Certain sectors appear to be under represented when compared with the profile of the Bank's lending within the EU. This is certainly true of electricity gas and water supply, whilst the railway sector is only one third the amount of the roads sector, despite a clear priority being given to the latter as part of accession priorities.

3. POLICIES & STRATEGIES – RELEVANCE

RELEVANCE *is the extent to which the project objectives are consistent with EU policies, the decisions of the EIB Governors, as well as the country policies. This chapter examines the key elements of these in turn before outlining the performance of the project sample.*

3.1 EU POLICIES AND OBJECTIVES

The rapid political and economic transformation occurring in the former member states of the Comecon[14] bloc towards the end of the 1980s created the first opportunities for bilateral trade contacts and agreements between the European Communities and many of the Eastern European states. As the pace of change gained momentum, the broader international community, including the EC, began to implement more active measures to work with these countries. Significant first steps include the G-7 PHARE programme, created in 1989, which was quickly followed by the EC PHARE

[14] Also known as CMEA: Council for Mutual Economic Assistance

instrument, created by the European Council in December 1989[15]. A further measure was the establishment of the EBRD in 1990 to aid Eastern European States in their transformation to the market economy. Widespread acknowledgement of the fact that the former Comecon States were historically a part of Europe and that closer political and economic cooperation was desirable for the benefit of all in the longer term, led to negotiations which concluded in the Europe Agreements[16], which were signed in the early to mid-1990s. These agreements aimed to provide an appropriate framework for political dialogue, to promote the expansion of trade and economic relations, to provide a basis for Community financial and technical assistance, and to provide an appropriate framework for the country's gradual integration into the Community. Henceforth, the signatory countries became known as "associated countries".

The accession process can be illustrated by the following timeline:

1993 – Copenhagen Criteria: The European Council meeting in Copenhagen stated in June 1993 that *"… the associated countries in Central and Eastern Europe that so desire shall become members of the European Union. Accession will take place as soon as the associated country is able to assume the obligations of membership by satisfying the economic and political conditions required."* The four criteria of membership defined by the Council, or the "Copenhagen criteria", formed the benchmark against which preparation for accession was measured[17]. Cyprus and Malta had applied to join the European Union in 1990, and the Copenhagen Council welcomed the Commission's intention to present its opinions on these countries in the near future. The subsequent Corfu, Essen and Madrid Council Meetings reinforced the conclusions of the Copenhagen Council.

December 1994 Essen Council: stated that the EU would embark on a programme to prepare for the accession of all countries with which it had concluded **Europe Agreements** and it set out a comprehensive strategy to prepare these countries for accession. The 1995 Madrid Council, in particular, stressed the need for applicant countries to adjust their administrative structures to ensure harmonious operation of Community policies after accession.

1994 – 1996: Poland and Hungary, then Romania, Slovakia, Latvia, Estonia, Lithuania and Bulgaria and, finally, the Czech Republic and Slovenia applied for membership. These countries were thenceforth called "applicant countries".

1997 Agenda 2000: This was an action programme proposed by the European Commission with the objective of strengthening Community policies and giving the Union a new financial framework for the period 2000-2006 with a view to enlargement.

The European Council meeting held in Luxembourg in December 1997 launched the enhanced accession and negotiation process for the applicant states based on the recommendations of Agenda 2000. The Council decided that future strategy would centre on **Accession Partnerships** drawn up between the EU and each applicant state, dealing with the priorities to be observed in adopting the *acquis communautaire* and the resources available for that purpose. Pre-accession aid was also increased substantially through the creation of two new instruments from 2000, which later became known as ISPA and SAPARD[18]. The existing PHARE programme was refocused to concentrate on the reinforcement of administrative and judicial capacity in the applicant states, and the adoption and application of the *acquis communautaire*.

3.2 NATIONAL/COUNTRY OBJECTIVES

As part of the enhanced accession process launched by the Luxembourg Council, each applicant country signed a tailored **Accession Partnership** with the EU. The Accession Partnerships formed the framework of the accession process for each country, setting out the key areas in which the applicant state had to make progress in priority areas identified by the European Commission together with details of EU financial support. The Partnership provided the basis for a number of instruments, inter alia, the National Programme for the Adoption of the Acquis (NPAA), the pre-accession fiscal surveillance procedure, the pre-accession economic programme, the pre-accession

[15] Council Regulation 3906/89 of 18.12.1989. PHARE : Poland and Hungary: Aid for Restructuring of the Economies.
[16] Europe Agreement establishing an Association between the European Communities and the individual country
[17] See Appendix 1
[18] Instrument for Structural Policies for Pre-Accession / Special Accession Programme for Agriculture and Rural Development

pact on organised crime, the National Development Plans, the Rural Development Plans, a national employment strategy in line with the European Employment Strategy, and sector plans necessary for the participation in the Structural Funds after membership and for the implementation of ISPA and SAPARD before accession. The adoption of the acquis was both a national objective for aspiring member states and a benchmark against which the Commission measured progress towards accession.

3.3 EIB POLICIES AND MANDATES

3.3.1 Pre-accession Mandates and Facilities

The Bank's pre-accession strategy for the twelve new member states developed in tandem with EU policy. Following the major political events in central and eastern Europe, the EU Council established a mandate for financing in Poland and Hungary, the first of a series of mandates which would later cover financing in the future pre-accession countries of central, eastern and south-eastern Europe. Prior to 1990, the Bank had also financed projects in Cyprus, Malta and Yugoslavia under regional mandates and country-specific protocols.

Up to the end of 1996, the Bank provided finance in central and Eastern Europe under mandate only, and these mandates were 100% guaranteed by the General Budget of the Community. The aim of the first two mandates, up to the end of 1996, was to allow the EIB to finance capital investment projects in countries undertaking fundamental economic reform. It was only after the Copenhagen Council of 1993 and the Essen Council of 1994, that the concept of "pre-accession" lending was applied. The third mandate of 1997, under a 70% Community Budget Guarantee, was established by the Council on the understanding that the Bank would, in turn, set up a complimentary pre-accession facility.

Operations with own resources under the CEE pre-accession facilities, established by the Bank's Board of Governors in 1998, were entirely at the Bank's own risk as they did not benefit from any Community or Member-State Guarantee. The intention was that the new pre-accession facility could be used for projects in investment-grade countries, thus allowing room under the mandates for non-investment-grade countries. Whilst lending under the facility was open to all countries authorised by the Board of Governors, projects in non-investment grade countries such as Slovakia, Lithuania, Bulgaria and Romania were still financed under mandate until these countries achieved investment-grade status.[19] Private-sector projects in countries lower than investment grade but for which the borrower could provide a guarantee acceptable to the Bank, could be financed under facility on a case-by-case basis.

The Bank also signed Framework Agreements with all individual states. These Agreements guaranteed the Bank's freedom to pursue, within the territory of the each country, the activities envisaged by its Statute.

It is not clear how the sizes of the financial limits for the early instruments were decided. It is likely that a number of factors were considered, including the decision taken at the Board of Governors' Annual Meeting of 1994 that external operations under Mandate from the Council should be subject to a ceiling of 10% of the Bank's average overall activity, as well as an assessment of the volume of business available in these countries based on sound banking principles. The size of subsequent instruments would then have then benefited from experience gained in working in the countries and the process of gradually building up reliable counterparts and intermediaries. Each envelope in turn was translated into lending targets to ensure that the Bank fully used the facilities available, and this engendered a culture of signature driven targets for pre-accession lending, possibly at the expense of disbursements (as discussed in §2.2 above) or indeed of policy related indicators (as discussed in §2.3 above and in §7) .

3.3.2 EIB Lending Priorities

Apart from implementing the Council Mandates for Central and Eastern Europe, and establishing the Pre-accession Facilities, EIB operational measures and targets to prepare for the accession of the twelve countries have been outlined in successive strategy documents. As early as 1990, a Board document entitled "The Role of the EIB in the 1990s" stated that

[19] Slovakia in 2001, Lithuania in 2002, Bulgaria and Romania in 2006.

"… on the external front, support for Central and Eastern Europe may well become a dominant preoccupation of the Community" and *"the effects … of the reforms in Central and Eastern Europe are particularly difficult to predict and could have a much more marked effect on the Bank's activities than (already) suggested."*

When setting up the first pre-accession facility in 1997, the Bank was able to review its operations under mandate and added for the first time an explicit consideration of what might be termed 'absorption capacity' in setting the size of the proposed envelope. However, in terms of lending policy, the beneficiary countries were treated very much 'en bloc' and the Bank reserved to right to retain maximum flexibility in terms of eligible sectors and operations.

In 1999, the Corporate Operational Plans (COPs) were introduced. At this stage, measures centred on continued support for candidate countries through the renewal of the Pre-accession Facility, but now focussed firmly on *"assisting countries to prepare for EU membership by facilitating adoption of the acquis communautaire."* Support was also envisaged for private sector development and privatisation, institution-building through support of local banking sectors, and possible application to lending under the Pre-accession Facility of the eligibility criteria applicable to core activity - including investment in human capital. Whilst the supporting documents provided an extensive review of economic development in the pre-accession countries, there was no obvious country or sector approach set out and the Bank continued to retain considerable policy flexibility.

Case Study – Project 3 (water supply and waste water treatment in the Czech Republic)

The project was one of a series of framework loans of the same type to eastern European countries, and monitoring and post signature approval procedures for the large number of sub projects were well rehearsed and effective. The project addressed both regional development and environmental priorities through the upgrading of water supply networks and sewerage treatment plants in numerous small Czech municipalities which would otherwise have been unable to obtain funding on an individual basis. Some of the larger sub projects were co-financed with EU grant instruments and the project is an excellent example of EIB support for EU priorities and the development of the *acquis communautaire*. The success of the project was strongly dependent on developing close links with a strong and competent implementation agency and the commitment of considerable EIB staff resources post signature.

From 2001 onwards, the Bank identified a limited number of top lending or operational priorities in its Corporate Operational Plans. From the outset, the preparation of Candidate countries for EU Membership became a stated top priority. However, it was accepted that the achievement of lending targets depended on market conditions in the countries, including such aspects as the number and volume of bankable and eligible projects, the willingness of the countries to further indebt themselves and the availability of state guarantees for infrastructure projects of public interest. A preference for grant financing over loans was also anticipated.

As a policy-driven institution, the Bank cooperated with the European Commission in carrying out its operations. Such cooperation was reflected in cooperation and framework agreements, extensive discussion between the Commission's and the Bank's services, ongoing contacts with representatives from the various Directorates General, Regio, Enlargement, TREN and others. There was also cooperation with the EC Delegations in the Accession countries.

3.4 ALIGNMENT OF EU AND EIB PRIORITIES

EU involvement in Eastern Europe began by assisting in the transition of these countries to stable democracies with functioning market economies. The EIB began operations in this context. Early operations were of a pioneering nature and the need was so great that activity of almost any kind was beneficial.

However, with the Council declarations in 1993 and 1994, EU and country involvement began to move towards a more focussed agenda aimed at achieving the Copenhagen criteria and the ultimate accession of the EU10 countries to the Union. Whilst much of the initial effort was directed towards the development of institutional and legal frameworks, the process of adoption of the *acquis* *communautaire* also highlighted those sectors which were in need of priority investment and, through the development of detailed Partnership Agreements, the EU and individual candidate states developed joint priorities for investment at individual country level.

Whilst declaring itself to be fully supportive of EU policies and priorities in the region, the Bank's approach was in practice more nuanced by practical constraints. As a result, when setting up its first pre-accession facility in 1998, the Bank continued to reserve for itself a wide mandate for intervention:

"The facility, as well as the lending mandate, shall be used in order to facilitate and accelerate progress in all sectors normally eligible for EIB financing, notably in areas of key European Union policy objectives."

Whilst this broad mandate was qualified by the need to 'take fully into account' the priorities being established in Accession Partnership Agreements, the Bank clearly intended to apply its normal EU lending priorities in the accession countries and saw itself as a facilitator rather than an initiator of change, to whom projects were 'brought' and assessed under various operational constraints over which it had little influence. This approach is set out in its review of lending policy in 2001. Given that projects being signed at that time would be the last to be fully implemented before accession, at least in EU10, the review provides in effect a 'report card' on over 10 years of lending. The main thrust of the review can be summed up as follows:

- The Bank aligns itself unreservedly with the thrust of EU policy and priorities.
- Key operational constraints limit the activities of the Bank in the region, principally;
    - i. budgetary constraints (linked to the Maastricht criteria),
    - ii. the limited supply of bankable projects (linked to the absence of complimentary sources of funds),
    - iii. the increased lead time for project development (linked in some cases to the application for EU grant finance).

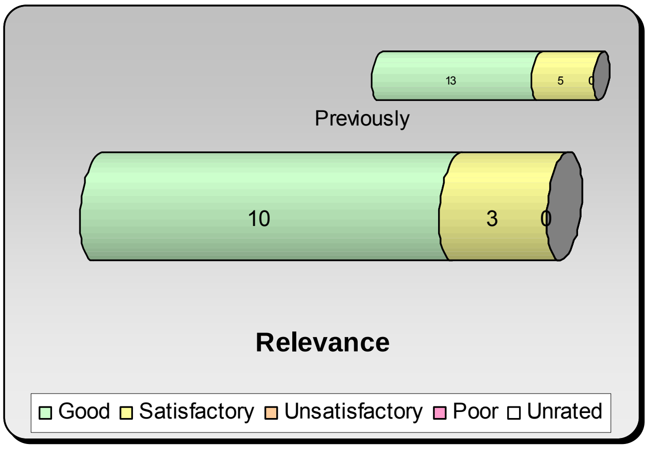
Interestingly, although the Bank reiterates that as a source of complementary finance its activities are driven by 'requests for EIB support' and that it does not provide 'macro-economic assistance or advice on policies', the document highlights two areas where the Bank directly intervened. Firstly in the currency markets, where the Bank seeks to support new capital markets by issuing bonds in the accession currencies and, secondly, in supporting municipality finance, which was identified as a key constraint to EIB lending in the environmental sector. The region is dealt with as a whole and there is little mention of particular countries or their constraints. The Bank was therefore pursuing a regional strategy.

The result was that in the process of putting into effect the same policies and priorities, the Bank recognised that the outcome would be more determined by practical operational constraints, and therefore continued to guard the maximum possible flexibility in its operations. Whilst this was not a divergence in policy, it was a divergence of approach which was always likely to lead to a divergence of outcome.

3.5 PROJECT RELEVANCE

PREVIOUSLY EVALUATED PROJECTS

During previous thematic evaluations, a large number of projects in central and eastern Europe were evaluated in depth. Although they were not examined specifically from the point of view of pre-accession lending, and in some cases were evaluated in a format which is not strictly comparable with current practice, they none the less form a useful body of evidence when viewed in the context of the current evaluation. Overall, 18 projects located in the New Member States had previously been evaluated in-depth as part of 5 thematic ex post evaluations. These projects had been financed by the Bank prior to accession to the EU. The ratings given to these projects against the standard evaluation criteria of relevance, effectiveness, efficiency and sustainability have been included as inserts in the charts below for ease of comparison. When comparing the two sets of ratings it should be borne in mind that as two distinct samples from the same population a degree of statistical variation would be expected. In addition, the projects previously evaluated span the whole pre-accession period, and some of the projects included are therefore relatively older than the sample chosen for this evaluation.



All projects evaluated in depth are considered to have contributed to one or more of the Bank's lending priorities at the time. Indeed, given the wide scope and overlapping nature of these priorities, it would be difficult not to so contribute. Whilst a wide mandate gives the Bank the maximum flexibility to operate in what are acknowledged to be difficult circumstances, it could be argued that the Bank is diluting its potential impact. None the less, the relevance of project 5 , being one of flood damage repair, is less obvious and although it has been rated as satisfactory, the relevance of this type of project, and disaster relief projects in general, at that time had no obvious place in the bank's established lending priorities.

All of the operations examined addressed one or more of the Bank's priority lending areas with the exception of project 5. At the time, any operation in the accession countries was considered to contribute to economic and social cohesion, thus guaranteeing the relevance of the operation. In addition 10 of the projects contributed to another EIB priority lending objective. Of these four were related to the TINA[20] transport network and one was a telecommunications projects. Five more addressed the environment and quality of life.

Project 8 was an industrial project and project 11 was an urban road bridge, both of which contributed to regional development but had no other policy relevance.

Project 5 concerned the provision of assistance for emergency flood relief. At the time there was no specific eligibility for this type of project and, further, since it involved the reconstruction of housing destroyed by flooding, it is debateable whether it represented activity in a restricted sector (real estate). However, the Bank's governing body has the discretion to declare individual operations, on a case by case basis, as being in the community interest and clearly took that view in this case. As a result the project is considered to be relevant.

EU policy at the time was increasingly focussed on the preparation for accession, with particular emphasis being placed on the adoption of the *acquis communautaire* in the transport and environmental sectors eligible for EU grant instruments. Whilst the Bank ascribed equal relevance to

[20] Transport Infrastructure Needs Assessment endorsed by the 3rd Pan-European Transport Conference in Helsinki in 1997

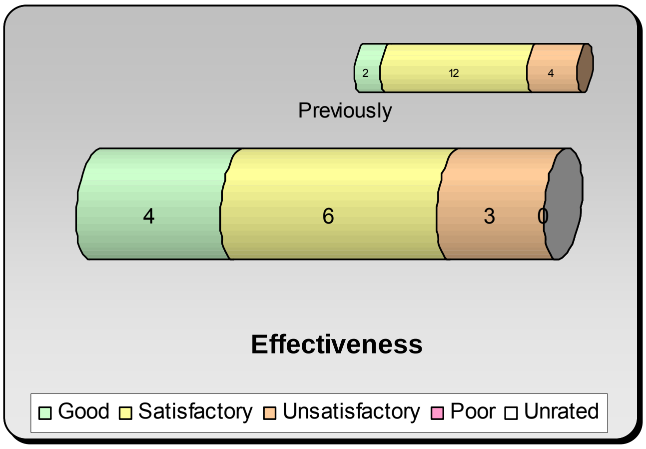
projects within these sectors, the Commission set out a clear hierarchy of priorities[21]. Whilst some of the projects examined relate well to these priorities, others (or parts of them) have a lower priority for the accession process. This aspect is discussed further in §7.

The ratings against **Relevance** for previously evaluated projected are broadly comparable, with no significant differences or discernable trend. A high proportion of projects examined were rated Satisfactory or better in both cases.

4. PROJECT PERFORMANCE

Project performance, relating to EIB's second pillar, is assessed using three core evaluation criteria, namely; Effectiveness, Efficiency and Sustainability, which are all rated individually. The Environmental performance of the project is reflected in these core evaluation criteria, but is also extracted and rated separately for emphasis.

4.1 EFFECTIVENESS



Project Effectiveness rates the extent to which the objectives of the project have been achieved, or are expected to be achieved, taking into account their relative importance, while recognising any change introduced in the project since loan approval. The evaluation looked at the following parameters: a) implementation: coherence with the technical description, timing, costs and procurement, b) operation: management and organisation of project operations, environmental performance, cooperation and coordination with counterparts.

The rating for the effectiveness criterion is good for four projects and satisfactory for a further six. Of the three projects rated unsatisfactory, two were roads rehabilitation projects which ran significantly over expected time and budget. Project 6 was a motorway concession which had extensive delays in setting up a less than ideal project finance structure.

The ratings against **Effectiveness** for previously evaluated projects are broadly similar, but with a slightly higher proportion of projects being rated Good in this evaluation. This may reflect the fact that promoters for later projects benefited from previous experience.

In looking at the extent to which individual projects achieved their objectives, the rating assessment concentrated on the physical and operational objectives of the project, but with due consideration of the inherent characteristics of each project. In general the Bank did not set any higher level objectives for the projects examined.

The majority of project promoters were public authorities, with two being private companies and one telecommunications company which was publicly owned but privately run. Seven of the projects examined involved the creation of

Case Study (Project 4) – Cogeneration plant for industrial supply

The owner of a large chemical manufacturing plant decided to secure his future supply of electricity and steam by building a co-generation plant onsite, and set up a joint venture with the local gas and electricity supply companies. The plant was completed largely on time and budget. The success of the venture depended on increasing demand from the manufacturing plant, and in the end the actual demand considerably exceeded projected figures to the extent that a further generation plant is now planned. The project was considered satisfactory overall despite the fact that the supplementary steam generation capacity of the project was never fully used as a local competitor, who had initially been expected to close, in fact continued to produce cheaper steam using a modified and more environmentally process.

21 Annual Report of the Instrument for Structural Policy for Pre-Accession (ISPA) 2000, COM(2001) 616 Final

transport infrastructure, three involved water and wastewater infrastructure and of the remaining three, two were industrial developments and one related to mobile telecommunications. The competence of the promoters to implement the projects varied. As might be expected, the private sector promoters achieved the majority of their implementation objectives, as did some public administrations, whereas others, whilst being technically competent, demonstrated poor planning and control.

4.1.1 Physical implementation

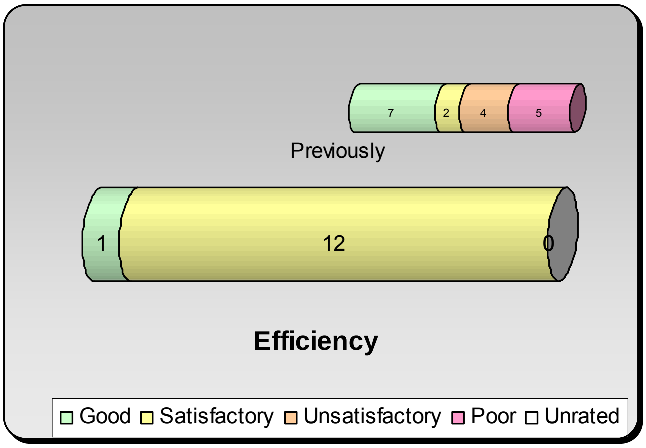
The majority of projects performed satisfactorily or better, with those implemented by private promoters rated as good (projects 4, 8 and 13).

Where there were problems in physical implementation (projects 1, 6 and 9), this tended to be as a result of poor project structuring, planning and design. Once construction started, problems were fewer although some construction contracts ran significantly over time and budget as well. Given that the economies of the countries in the region were in transition, and that several of the promoters were acknowledged to be inexperienced, insufficient allowance was made at approval stage for possible cost and time over runs. This was despite the fact that the risks were clearly identified in appraisal documentation.

4.1.2 Operational Performance

In general the operational performance of the projects examined was satisfactory or better and most promoters were experienced operators. In most of the cases where the achievement of a certain level of demand was a project objective, the projects attracted demand in excess of that predicted at approval stage and this was considered beneficial. The exception was project 11, where the capacity of the new infrastructure was already being approached when the project was examined ex post.

4.2 EFFICIENCY



Efficiency considers whether the project objectives are achieved in a manner that represents the efficient use of resources. Efficiency is also one of the main considerations when choosing between projects to allocate scarce resources.

All of the projects examined were considered to represent the efficient use of resources. Project 3 was considered to have a particularly high return on the investment made. Of the remaining projects, only project 2 exhibited a low rate of return, but this was considered to be offset by intangible benefits arising from the transfer of travel from private to public modes. Whilst all projects were considered at least acceptable in economic terms, none except project 3 exhibited what might be described as 'premium' returns.

Ratings against **Efficiency** for previously evaluated projects are substantially different, with previous evaluations giving a more polarized view both at the upper and lower end of the rating scale. The projects rated Poor were amongst the first transport projects carried out by the Bank in these countries and economic efficiency was adversely affected by difficulties in estimating both costs and traffic levels in an operating environment which was largely unknown. This situation was found to have improved for later projects.

The new sample contained a variety of project types and sectors and the efficiency indicators examined were chosen accordingly. For public sector transport infrastructure projects the economic internal rate of return (EIRR) was examined. Benefits largely stem from savings in travel time, but can include other aspects such as safety benefits. These benefits are valued and compared to the cost of the project over its economic life. Environmental benefits were not quantified but were considered in the context of possible enhancement or reduction in the EIRR. In line with sector practice, the economic benefits were not assessed on a quantitative basis for water supply and treatment projects, where economic efficiency was considered to be the least-cost achievement of the stated environmental objectives. For commercial projects where users were expected to pay for the service provided, efficiency was gauged by the financial performance of the operator. In the special case of project 5 (emergency flood relief), a qualitative assessment was made of the efficient use of resources.

4.2.1 Project performance

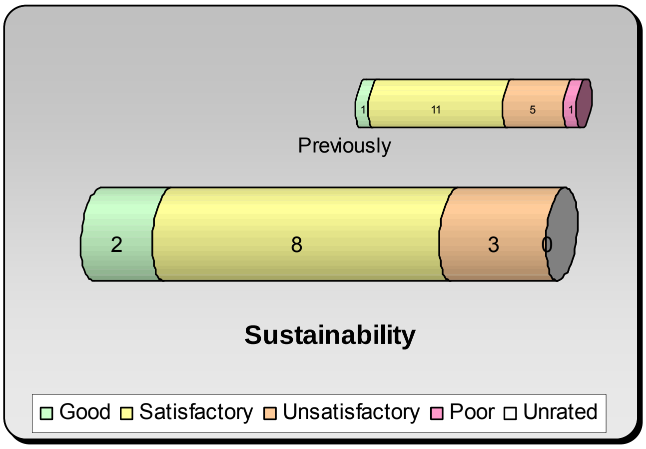
Most of the projects examined exhibit economic rates of return in the range 10 to 15% and are therefore likely to have a positive net present value to society. Whilst this is an acceptable return, it could be argued that higher returns should be targeted in rapidly developing countries. Rates of return in excess of 15% are considered Good, or ‘premium’ returns for the purposes of this evaluation, but none of the projects examined were considered likely to fall into this category, with the exception of project 3.

Projects 1 and 9 were roads rehabilitation projects containing many sub projects, some of which were claimed to have higher returns (up to 30%) but an overall ‘average’ figure was not provided. However, the view was taken ex post that concerns about the economic life of these projects were likely to reduce these to a similar level to the other projects assessed.

The only project exhibiting a return of less than 10% was project 2, which was a metro extension. The approval of this project was on the basis that intangible environmental benefits arising from the transfer of travellers from more polluting modes of travel would raise the rate of return to an acceptable level. Whilst this argument is accepted ex post, it is one which has been commonly used for many years as a form of ‘subsidy’ in favour of public transport investment and, given the increasing importance of travel by less polluting modes of transport, it is one which the Bank should now seek to put on a more secure evidential basis. In this case, the promoter was of the view that most passengers using the metro were also former public transport users, and whilst this would still give rise to benefits when compared with the use of diesel buses, they would be less substantial than transfer from private cars.

Three projects had no quantified rate of return. Projects 3 and 7 were water supply and wastewater treatment projects, where social benefits were likely to far outweigh costs, and project 5 was a flood relief project where the calculation of a return was not possible.

4.3 SUSTAINABILITY



The sustainability criterion looks at the probability that the resources will be sufficient to maintain the outcome achieved over the economic life-time of the projects, and that any risks can be managed.

Most of the projects examined were considered to be sustainable in that there was minimal risk that the use of the projects would be adversely affected during their economic life. Projects 2 and 7 were considered to be particularly secure, representing essential services within strong municipal frameworks. The investments in projects 1, 9 (roads) and 5 (flooding) were considered to be at significant risk during their economic life that project benefits will be reduced by outside factors.

The ratings against **Sustainability** for previously evaluated projects are broadly similar, with possibly a slight improvement overall recorded in this evaluation. The project rated Poor was the first operation in a series of roads investments of which project 9 is the third, indicating a gradual improvement, but still not to acceptable levels.

In assessing the sustainability criterion it is necessary to take a view on the importance of various risk factors to the project. Since no project is entirely without risk, this is a question of degree, and since there can be no real quantification of risk of this nature, the approach taken is that only those risks which stand out as fundamental to the future success of the project are considered. For 8 of the projects examined no such factor stood out and projects 2 and 7 were considered to be particularly secure. These were essential public services within strong municipal frameworks. Project 2 was part of a well funded and successful metro network in a major city, and project 7 represented the upgrading of essential municipal infrastructure in a major municipality. The importance of these investments within the direct control of large stable municipal authorities was considered to make their future particularly secure.

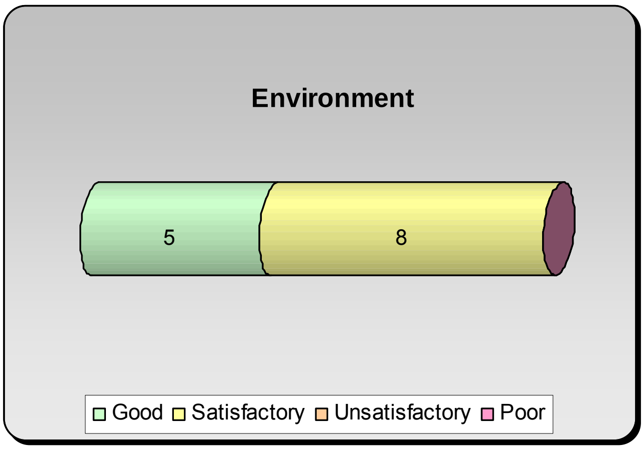
Case Study (Project 6) – Motorway concession

The project involved the construction and operation of 136 km of motorway. The 40 year concession was awarded following a lengthy period of discussion and negotiation. After eventual signature of the agreement, the project was completed ahead of schedule. The Bank's role in unlocking the project was instrumental in getting the project started but ex post there remain some doubts as to whether the project represented value for money. Traffic levels have now exceeded expectations, although a government decision to introduce a vignette system for trucks has complicated the comparison. Indeed government interference is the main risk factor since the resulting increase in truck traffic has brought forward likely maintenance requirements and according to the concession company it was not fully compensated for the resulting changes to its business.

Project 5 involved the reconstruction of housing damaged or destroyed during flooding of a major river. The project was unusual in nature in many respects, but the main risk in terms of the project's sustainability was that housing was reconstructed in situ without any obvious measures to reduce the risk of similar flooding recurring. Although the new buildings are more robust, with flood return periods reducing there is a clear risk of further damage within the economic life of the project.

Projects 1 and 9 represented extensive roads rehabilitation programmes in different countries consisting of many geographically dispersed sub projects. Both operations were part of a series of investments by the Bank, and both were partly co-funded by EU grant aid. Road maintenance in both countries is recognised to be underfunded at the time, and remains so. Although the situation has slowly improved, it is not at a sustainable level and there is therefore considered to be a risk that the economic life of the projects may be reduced.

4.4 ENVIRONMENT



Environmental and social impact assesses the project from an ecological point of view. This criterion examines the immediate impact of project implementation and operation, but also extends to the wider view of the project and its long term consequences on carbon emissions, energy efficiency, green spaces, involvement of local communities, transport, local employment, social cohesion, etc. where these are relevant.

Consideration of environmental factors is already included within the internationally agreed criteria of relevance, effectiveness, efficiency and sustainability included above. They are repeated here separately firstly to emphasise the importance the EIB attaches to environmental and social matters, and to clearly distinguish environmental factors from those other considerations taken into account when rating relevance, effectiveness, efficiency and sustainability.

Most of the projects examined where associated with physical infrastructure and within the EU would have required an Environmental Impact Assessment according to EU regulations (Directive 97/11/EC). Whilst the transcription of EU into local law was by definition in a state of flux during the pre-accession period, from an early stage the Bank took the view that, in addition to making its own environmental assessment, it would apply the principles of EU directives regardless of the progress of particular countries in adopting the *acquis communautaire*. The main problems in putting this policy into practice were associated with projects which within the EU would have fallen under Annex II of the directive and where normally the competent authority would decide on the requirement for a formal EIA.

Six of the projects examined were considered to have net positive effects on the environment. These included the three water sector projects (projects 3, 5 and 7) a public transport project (projects 10) and a motorway project (project 6). Project 6 removed substantial traffic, including long distance trucks from a whole series of towns and villages that had grown up alongside the existing national road which was replaced by the motorway. In addition, project 4 involved the replacement of power and steam generating capacity with a more efficient and less polluting plant.

Case Study (Project 10) – New Saw Mill

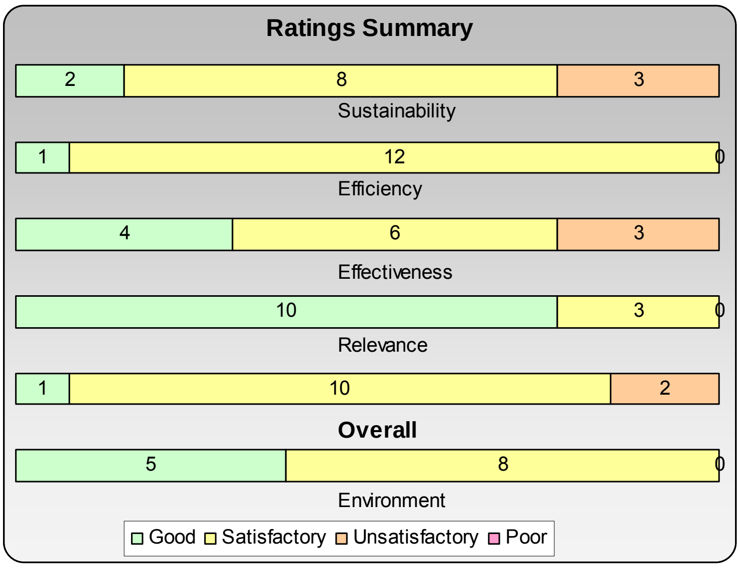
The project was located in a rural area close to extensive natural timber supplies. The promoter was an experienced EU operator and active member of the World Wildlife Fund. Environmental protection and sustainable forest management were therefore at the core of the plants design, which included the use of waste chippings to generate electricity and the installation of advanced filters to meet EU emission standards. An EIA was undertaken under local law. The promoter made considerable efforts to agree terms with the state railway company to transport its produce out of the country, but in the end he had to resort to the use of road haulage. The Bank attempted to intervene at a project level but without success although the promoter felt the Bank could have applied more pressure at a higher level.

The two roads rehabilitation projects (projects 1 and 9) were not subject to an EIA on the basis that the works involved the improvement of existing roads online, whereas the Bank insisted that the bridge project (project 11) was the subject of proper public consultation - as a result of which, additional mitigation measure were introduced. Project 13 involved the extension of mobile phone coverage by the erection of additional masts. These were placed as far as possible adjacent to existing transmission nodes and both the new technology and the increased density of the network actually reduced the intensity of electromagnetic radiation in many instances.

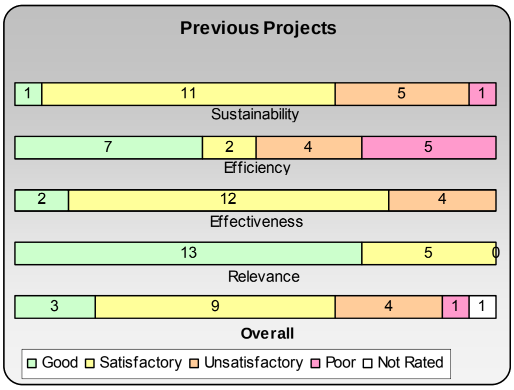
The remaining projects were considered to have adverse impacts overall, but mitigated to an acceptable level. In the course of the approval process, all projects were subject to an environmental review by the Bank, in which compliance with local, state and federal law was verified and confirmation sought that all relevant permits were obtained. No project evaluated ex-post raised significant concerns from the environmental point of view.

4.5 OVERALL PROJECT RATINGS

Ratings on relevance and project performance: *As outlined in the introduction, the operations were evaluated on the basis of internationally accepted evaluation criteria of Relevance, Efficacy, Efficiency and Sustainability. These individual ratings are considered together to produce an overall rating for the project. This is not an arithmetical exercise, and reflects the extent to which individual aspects contribute to the whole on a case by case basis. Environment is rated separately, but is already accounted for within the four main ratings.*



The overall ratings confirm that the majority of projects which the Bank financed in pre-accession countries performed well under difficult operating conditions. Relative deficiencies were linked to cost overruns and delays which were not anticipated and the inability to tackle a particular sectoral problems.



Projects examined as part of the current evaluation also have tended to perform better than those older projects evaluated as part of earlier themed evaluations. This is particularly marked for the Efficiency rating, and is probably indicative of a general improvement in project identification and selection as a result of increasing experience of working in the region.

4.8 EXTENDED ANALYSIS – PROJECT COMPLETION REPORTS

In order to further extend the scope of the analysis EV have examined the self evaluation (Project Completion Report) information completed during the evaluation period.

Extended Scope: Survey of Self Evaluation Procedure through Project Completion Reports (PCRs) for New Member States

62 PCRs (9 Baltic States, 16 Central Eastern Europe, 7 Slovenia, 20 Poland, 10 South Eastern Europe), which were issued by the Bank between 2004 and 2007, were included in this Completion Report Survey. The sub-sectoral split of the PCRs is led by "Transport, Storage & Communication" (35), and followed by "Manufacturing" (8) and "Electricity, Gas and Water Supply" (6). Other sectors include: "Construction" (5), "Others" (5), "Human Capital" (1) and one Global Loan (1). By monitoring category, 8/10/25 projects were classified in category 1/2/3 respectively and 18 projects were not classified.

RATINGS

- Value Added Pillar 1 -

The contribution to EU objectives was considered "high" in 52% of the present desk review portfolio, "medium" in 31%, and as "moderate" in 6% of the projects in the sample. 11% of the PCRs did not receive any rating for VA Pillar 1 and none were judged "not acceptable".

Country	Number of PCRs	Value Added Pillar 1				
		High	Medium	Moderate	Not acceptable	Blank
Baltic States	9	2	6	0	0	1
CEE	16	10	4	1	0	1
FYR	7	3	2	0	0	2
Poland	20	13	4	1	0	2
SEE	10	4	3	2	0	1
TOTAL	**62**	**32**	**19**	**4**	**0**	**7**

- Value Added Pillar 2 -

The projects' quality and soundness were considered as "good" in 50% of the projects, "satisfactory" in 39%, and "unsatisfactory" in 5%. There were 4 projects that were not rated under the VA Pillar 2 and none were judged "not acceptable".

Country	Number of PCRs	Value Added Pillar 2				
		Good	Satisfactory	Unsatisfactory	Low/Not acceptable	Blank
Baltic States	9	5	3	0	0	1
CEE	16	6	7	3	0	0
FYR	7	7	0	0	0	0
Poland	20	10	8	0	0	2
SEE	10	3	6	0	0	1
TOTAL	**62**	**31**	**24**	**3**	0	**4**

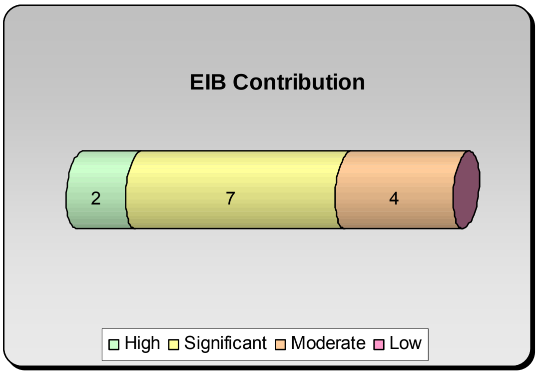
- Value Added Pillar 3 -

Value Added Pillar 3, "Financial benefits obtained by use of EIB funds" was reported in only five of the PCRs analysed (where a qualitative assessment was offered).

Key Findings:

- A majority of the 62 projects (52%) were deemed to contribute "highly" to EU objectives;
- 89% of the projects reviewed were considered "satisfactory" or better from a project quality/soundness perspective.
- 3 of the 62 PCRs did not contain any information and 1 PCR concerned a project cancelled after signature.
- Finally, the Bank's self-evaluation procedure is a key step in the institutional learning process, and while yet not fully consistent, based on this review the Bank's services are increasingly making use of the specific *learning space* provided during the self-evaluation process.

5. EIB CONTRIBUTION



The contribution which the EIB makes to the achievement of economically productive projects is both financial and non financial. It is assumed that if the Bank is able to conclude an operation with a particular promoter, that this contribution must by definition represent a positive contribution. This criterion is therefore rated on a different scale from previous evaluation questions, and all ratings are positive (high, significant, moderate and low).

Ex post, the Bank's contribution varied considerably, and there was no direct correlation between a high contribution and a successful project. In some cases a Good project resulted from a relatively modest contribution by the Bank (projects 7 and 8), suggesting that the project was fundamentally sound anyway. In other cases, aspects of the project outcome were Unsatisfactory despite a significant contribution by the Bank (projects 1, 6, 9 and 11).

5.1 FINANCIAL CONTRIBUTION

For the majority of projects examined, IFI support was the only available source of long term funding. The Bank's financial contribution was therefore high, giving the Bank considerable potential influence over the projects. In most cases these projects were also part of a series of investments in a well defined programme, some of which also benefited from EU grant finance. This combination of circumstances gave the Bank considerable leverage not only over the project but also over the sector.

Those projects where the Bank's financial contribution was less critical tended to be private sector projects (projects 4 and 8) where alternative commercial sources of finance were available, but where the Bank's terms were more attractive overall, taking account of the cost of the loan as well as the flexible terms and maturities on offer. The other cases were a strong municipality (project 7) with access to own funds and municipal bonds, and project 5, where the Bank lent directly to the national government.

The Bank's financial value was also critical for one private sector promoter (project 6) where the Bank demonstrated considerable flexibility in providing a zero coupon bond that was instrumental in creating the conditions which allowed commercial banks to complete the project finance structure for the PPP concession contract, effectively unlocking the project.

Case Study (Project 13) – Mobile phone infrastructure

The borrower was a publicly owned mobile phone operator who wished to expand the penetration of the latest GSM technology. This involved substantial infrastructure investment both to increase network density and to upgrade existing telecommunications nodes. At the time of the operation, competitors were beginning to establish themselves in the market and local law did not permit commercial banks to fund a project of this scale and importance. The Bank's terms were viewed as the most attractive of available IFI funding sources. EIB had already established a good working relationship with the borrower through two previous operations. The Banks involvement was seen as enhancing the image of the company and has helped in negotiations with EU equipment suppliers who were vital to the project. Ex post, the borrower specifically complimented the Bank on its contribution to the project.

5.2 INSTITUTIONAL AND TECHNICAL CONTRIBUTION

The main contribution of the Bank to other aspects of the project tended to be through the enforcement of the Bank's policies on procurement and the environment which, in most of the cases examined, required a considerable staff resource input. In many cases the Bank also insisted on the appointment of experienced international consultants to assist the promoter in implementing the project.

These contributions were mainly made at project level and where occasionally a suggestion was made at appraisal for the introduction of a conditionality extending beyond the project, this was either not followed through or diluted (see §6 below). As a result, the outcome of a project was sometimes affected by sectoral issues which the Bank did not directly address. This was the case in projects 1 and 9 where it was felt that the Bank might have had considerable influence in resolving the long term under funding of maintenance in the roads sector. In both cases, the project examined was the third in a series of similar projects with the same promoter. The lack of maintenance funding was identified as a risk at approval stage, but no concrete measures were taken to mitigate this risk.

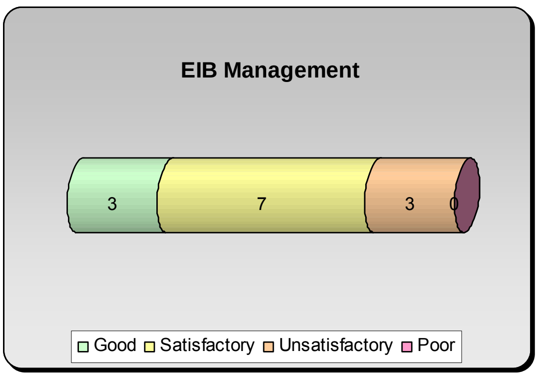
Other examples were project 10, were it was felt that a more transparent financial framework for the city's public transport would have been of benefit, project 9 where basic traffic data was not being collected on a regular basis, project 11 where the promoter had failed to tackle public transport provision in new city centre transport infrastructure, and in project 8 where the promoter was not able to resolve rail transport issues with the state railways. Although project 5 was somewhat of a special case, it was also felt that the Bank could have had more influence on future flood prevention and mitigation measures.

It was clear from consultations with operational staff that considerable efforts were often made at project level to indirectly influence supra project issues, but with limited success. In no case did the finance contract contain any disbursement conditions linked to sectoral issues, even when the borrower was a sovereign or sub sovereign entity. It must be concluded that action at individual project level is unlikely to be sufficient to overcome supra project problems.

The notable exception to the above general comments is the way in which the Bank opened up the potential to finance Municipalities and the numerous small environmental projects which made an important contribution to the accession process (projects 3 and 7). In certain sectors (water for example), there was close policy alignment between the Bank and the Commission, allowing a larger sectoral view. This is a good example of the potential impact which the Bank can have in overcoming obstacles at a sectoral level and clearly indicates that coordinated and concerted action is needed upstream of individual project appraisal.

The above comments relate to approved projects which had already in effect met the Bank's bankability requirements. Given that in most cases the attractiveness of the Bank's funds gave it considerable influence during the pre-accession process, it could be argued that the Bank, particularly if it were to act in concert with other IFIs and the Commission, could have done more to develop sectors and institutions which would in the longer term have increased the pipeline of bankable projects and allowed the Bank to focus more on accession priorities rather than filtering bankable projects from the available pipeline.

6. EIB PROJECT-CYCLE MANAGEMENT



EIB project cycle management has been developed over a long period of time and is systematic, structured and well adapted to the vast majority of the Bank's operations. In the majority of cases projects were well handled from a procedural point of view, and 10 out of the 13 projects examined were rated satisfactory or better. Of the three projects which were considered unsatisfactory, it was felt for projects 1 and 9 that although sector difficulties were correctly identified, insufficient allowance was made for these within the subsequent Bank operation. It was also felt that whilst significant reservations were expressed regarding Project 6, the Bank decided none the less to support the project. In addition, a number of individual issues were highlighted which could assist in the management of future project in transition economies, and these are discussed below.

6.1 PROJECT IDENTIFICATION AND SELECTION

The Bank has good relationships with many of the main counterparts, who are often repeat borrowers. Most of the projects evaluated in-depth were identified responding to requests from existing customers, government agencies or as a follow up from earlier projects, although there were also notable examples of the Bank identifying new counterparts and actively seeking projects in priority sectors. Once identified, the projects went through the initial internal screening process, which largely concentrated on the bankability of the project. The net result of this essentially project orientated process, as discussed elsewhere, appears to have been that bankability factors predominated over policy priorities and that this resulted in an under representation of the Bank in certain sectors (for example the energy and railway sectors in this case) where conditions were difficult, and also a degree of misalignment of outcomes with policy intentions (in relation for example to co-funding with the Commission). There is therefore a need for the Bank to refocus its project identification and selection efforts towards a more strategic level of intervention aimed at addressing country and sectoral constraints which are likely to limit the supply of bankable projects.

6.2 APPRAISAL

Project appraisal was usually well-structured and systematic, although the approach varied considerably by sector. In most cases the appraisal documents gave a knowledgeable and balanced view of the project and its sector and correctly identified the likely risk factors.

However, having identified the risks, these were not always followed through to project implementation. In the case of projects 1 and 9 the appraisal identified weaknesses in the sector and with the promoter, but then made insufficient allowance for these during the projects implementation. In several cases (projects 1, 2, 5, 7 and 10) suggested conditions for addressing weaknesses were either not followed through or watered down (as for example in project 7 where a proposed disbursement condition relating to tariffs was included as an information requirement). In fairness to the Bank's project teams, once a specific project proposal is brought forward for assessment, it is much more difficult to influence sectoral issues if they have not already been dealt with at a more strategic level.

Project 6 was a complex concession project to which the Bank came relatively late in the process of financial close. Without the Bank's intervention, the project, which had already been delayed by several years, would probably have to have been cancelled and re-tendered. In appraising the project the Bank was faced with some difficult issues, but decided to support the project rather than subject it to further delay. This may well have been the correct decision, but it was not one supported by any rational analysis in the appraisal documents.

Case Study (Project 1) – Roads rehabilitation programme

The project was the third in what eventually became six operations involving the rehabilitation of hundreds of kilometres of national roads which required substantial reconstruction following years of maintenance neglect. Parts of the project were being supported by ISPA and the Bank concentrated on the remainder. The appraisal of the project was processed very quickly with only 6 months elapsing between project identification and signature. Whilst it was a repeat operation, it was felt that this was rather a short timescale given the complexities of the project and the sector. The project was structured as an investment project, despite the fact that many sections were clearly at an early stage of preparation and were likely to be subject to change. Four years after signature, following substantial implementation difficulties, the scope of the project was increased from 600 to 780 kilometres and reorientated towards different priority corridors. The Bank accepted this change without substantial comment and within six months had signed a further similar operation. The risk of delays and cost over runs, together with chronic under funding of maintenance were identified as risk factors, but insufficient allowance was made for these in the operation structure and no special provisions were included in the finance contract relating to maintenance funding. By contrast, the Commission's financing memorandum included a requirement for a specific repair and maintenance programme.

Six of the projects examined were repeat projects of one sort or another. Within the EU it might well be appropriate to modulate the effort expended in appraising these, since many of the issues would already have been explored. However, in situations were operations are more difficult, repeat projects can give rise to their own additional problems related to the ‘absorption’ capacity of the promoter, the sector and even the country. The apparent absorption capacity problem of Romania was referred to in §2 above. It is also particularly important in these circumstances that sufficient time is taken to ensure that lessons learned from previous projects are applied to subsequent operations. Where the implementation of projects and programmes can take many years, the process of institutional learning and handover must be formalised to a greater extent than at present where changes in personnel may have contributed to a lack of awareness of cumulative problems over several operations. It was felt in general that the appraisal of repeat projects underplayed these issues.

6.3 PROJECT IMPLIMENTATION/FINANCING ARRANGEMENTS

Most of the projects’ promoters were satisfied with the EIB’s internal handling and procedures to support a smooth project implementation, and some were expressly complimentary (projects 2 and 13). In addition the Bank’s intervention in project 6 by proposing a zero coupon bond arrangement was critical to overcoming bankability problems which had stalled the project for several years. In general all promoters appreciated the Bank’s flexibility in matching disbursement to individual needs. In one case (project 3) nine separate loan tranches were signed.

Changes in project scope were sometimes either not recorded or not reflected in contract amendments (projects 2 and13) and, as discussed above, proposed conditionalities were not always included or followed through. In the case of project 5 the Bank imposed a condition that reconstructed houses could not be resold for 15 years, but this was subsequently overturned by appeal at law.

6.4 MONITORING

Of the projects which were intended to be fixed investments, the Bank appeared to be unaware of some of the changes made to the scope of the projects during implementation (projects 2 and 13). In other cases the Bank accepted significant changes to the scope of the project post approval with no documented reassessment of the quality of the project (project 1).

For those projects where some form of post signature approval process could be expected, the Bank’s approach varied considerably from a clear framework laid out in advance within the finance contract (project 3) to a reliance on progress reporting by the promoter which in some cases was not respected (projects 7 and 13). Project 5 represented a form of emergency relief, and the final scope of the project was not communicated to the Bank until after completion.

Case Study (Project 7) – Municipal infrastructure

The project comprised two distinct components; a water and wastewater component co-funded with ISPA, together with the upgrading of two main city roads and their access roads. A PIU was set up for the ISPA funded components but did not cover the roads component which formed part of the Bank’s project. There was no evidence in the Bank’s files of liaison with ISPA during monitoring and the Bank did not separately monitor the roads component of the project. The agreement of tariff policy had been suggested as a disbursement condition at appraisal but was only included as a special undertaking and then never followed up.

For most of the projects examined, the Bank had asked for some form of enhanced progress reporting. This was usually accompanied by the appointment of international consultants who were responsible for progress reporting and in general the requirement was respected. However, the extent of the Bank’s follow up varied considerably. In some cases (projects 1, 3, 9, 11 and 12) Bank staff spent considerable time and effort during the implementation phase. These projects were generally large programmes of small investments requiring some form of post signature approval, or projects with particular problems had been encountered (project 11).

In other cases the Bank’s follow up was much lighter or non existent. For the three private sector projects (projects 4, 8 and 13) this approach was probably justified, although in the case of project 13 the Bank appeared to be unaware of significant changes which had been made to the scope of the project. In cases where the project was co-funded with EU grant instruments (projects 1, 3, 7, 9 and

12), the Bank tended to partition the project, and relied on ISPA to monitor its own sections but without any apparent coordination or liaison between the two in terms of progress reporting. The Bank then followed up its own sections, except in the case of project 7 where there was no apparent follow up of the Bank's roads component. In other cases the Bank's input was significantly affected by a high turnover of staff and a lack of formal handover procedures.

Completed Project Completion Reports (PCRs) were examined for the in depth sample. All but one were completed and most of these gave a good picture of the project at completion. However, in rating the quality of the project there was a tendency to be optimistic compared with the finding ex post. In addition, all PCRs completed in the 'new' format were also examined. This therefore limited the search to the period 2004 to 2007 for which 62 PCRs were identified. In general the self assessments present a more positive view of the operations during the period than that made of the sample selected for ex post evaluation, with over 90% of projects being rated in the top two categories for quality and soundness, and over 50% being rated in the top category.

When compared to similar exercises undertaken during recent ex post evaluations, the picture is similar, with over 90% being rated in the top two categories, but with an even higher proportion in the top category (generally in excess of 70%).

7. PREPARATION FOR ACCESSION

The extent to which the Bank had contributed to assisting beneficiary countries with their pre-accession objectives was identified as a key issue for this evaluation.

Given the nature of the Bank's databases and records, this question could initially only be answered for the sample of projects chosen for in depth evaluation. However, it was considered important enough to merit investigation on the basis of a larger sample. Some 30 further projects were therefore selected for extended scope analysis with the aim of providing a broader view of the issue than can be provided by the smaller in depth sample of projects. These were projects which were financed prior to accession and due for completion reporting before the end of 2007. The projects were located in nine of the ten east European countries which joined the EU on 1 May 2004 and one in January 2007. The only country not represented in the sample was Slovenia, as the remaining projects in that country were very similar to the two projects already included in the in-depth analysis. The operations analysed cover the private and public sectors, direct (investment) loans and framework loans and the sectors broadly mirror the overall activity for the 12 NMS prior to accession. The projects covered in this extended analysis are already included in the overall statistics on pre-accession EIB activity, on which the Portfolio Review[22] for this evaluation is based.

The analysis of the extended sample was based on a review of the appraisal, finance-contract, monitoring and disbursement files held in the EIB Records Management Unit for each project, together with a consultation of the EIB Serapis application.

The following indicators were used as the basis for assessing the Bank's contribution to the accession process. The list may not be exhaustive, but it has been chosen to reflect as far as possible the overall process using data which are available from the Bank's archive.

7.1 SUPPORTING SECTOR IMPROVEMENT TOWARDS EU STANDARDS

All of the projects examined were relevant, and in some cases highly relevant, to EIB lending policies and priorities. In addition, by pursuing its normal approach to environment and procurement issues, the Bank made some contribution to raising awareness of EU requirements in these areas, at least at project level, and therefore contributed to the accession process. Individual projects also contributed directly to upgrading vital infrastructure to EU standards. This was particularly true of projects 3 and 7 which made significant direct contributions to achieving EU water treatment standards. Other projects also made some contribution to the achievement of the Copenhagen criteria, particularly the adoption of the acquis communautaire, but could not be described as priorities for the accession process.

[22] See §2

In some cases the Bank worked hard to overcome operational constraints and for example made considerable efforts to unlock the potential for municipalities to fund vital environmental infrastructure. Through a series of carefully structured and monitored framework loans throughout the region the Bank made a significant contribution to the adoption of the acquis communautaire in this sector.

However, as already mentioned in §2, looking at the lending portfolio as a whole, the Bank's intervention has tended to relatively favour those countries which are already further developed and sectors which were less difficult. Also, as mentioned in 5.2, the Bank did not tackle certain sectoral issues which limited the benefits of individual projects.

The Bank's approach therefore seems to be neither wholly the passive receiver of projects, which are then filtered according to existing operational constraints, nor the developer, pro actively unblocking existing operational constraints. The projects which the Bank has supported undoubtedly make a positive contribution to the accession process, but one is left with the impression that even better results could have been obtained by concentrating more effort at country and sector level.

7.2 SUPPORTING THE DEVELOPMENT OF FINANCIAL MARKETS AND PRODUCTS

The Bank's aim of seeking to contribute to the development, deepening and diversification of local capital markets in order to make local currency available for disbursements in support of productive investments is seen by the Bank as bringing key added value to its lending operations. Up to 2002 some EUR 16.7bn had been disbursed in the accession countries of EU12 and some EUR 1.6bn of bonds had been issued in local currencies, of which EUR 900m had been disbursed, representing some 5% of total disbursements by the end of 2002. Treasuries had been established in CZK, PLN, HUF and SKK.

Of the 43 projects covered by the analysis, 25 were disbursed solely in EUR. The remaining 18 were disbursed in USD, local currency, DEM, CHF, ITL or a combination of any one of these currencies with the EUR. There are only two countries where projects were disbursed wholly in local currency - the Czech Republic and Slovakia.

Borrower's preference for hard currency was likely to have been driven by a number of factors, including the demands of international contractors, but it can be concluded that the availability of disbursements in local currencies made a positive, if relatively small, contribution to the accession process.

The Bank has also been active in trying to unlock public borrowing constraints through the use of PPP project structures; although these efforts were perhaps less successful in that there were few such projects in the portfolio and the structure of the project examined in depth (project 6) was less than ideal.

7.3 SUPPORT FOR THE IMPLEMENTATION OF EU DIRECTIVES

Generally speaking, if the Bank requires borrowers to comply with any special requirements, these are reflected in the finance contract by means of conditions. The presence or absence of these conditions was therefore examined as an indicator of the extent to which the Bank was actively involved in developing country and promoter capabilities in specific areas of the *acquis communautaire*.

Of the extended sample of 30 projects, five did not have any non standard conditions precedent to first or subsequent disbursements.

Conditions of first and/or subsequent disbursements: Environment

The conditions of first and subsequent disbursements related to the Environment were included in 10 finance contracts. These ranged from the recruitment of an external environmental expert to receipt by the Bank of confirmation of environmental approvals and permits from relevant authorities prior to commencement of works.

Conditions of first and/or subsequent disbursements: Procurement

The conditions of first and subsequent disbursements related to procurement were included in nine finance contracts, and ranged from compliance with Directive 93/38/EC to the application of ISPA procurement rules.

The conditions of disbursement, which are enforced by the Bank, illustrate the importance attached to technical assistance, PIUs, environmental expertise, environmental approvals and permits, and international tendering.

7.4 COOPERATION WITH THE COMMISSION AND IFIS

The extent to which the Bank cooperated with other funding agencies, and in particular the European Commission, was taken as an important indicator of a targeted and coordinated approach to lending priorities prior to accession. The extent of the Bank's cooperation with the Commission is an aspect of the Bank's activities which is continually emphasised as a key component of the Bank's approach. However, it is also an aspect of the Bank's activity which is most difficult to research because information on co-financing is recorded at project approval, but is subject to change due to decisions subsequently taken by the borrower or an IFI, and these changes are not systematically recorded in the Bank's databases. The presence or absence of information at approval is not therefore a reliable indicator, and the Bank's monitoring files have to be examined in each case.

Co-financing with IFIs

Out of 43 projects examined in total, there were seven cases of co-financing with another IFI, and another four cases where either IFI co-financing was planned and did not materialise, or where an IFI financed related projects. In five of the seven cases, IFI involvement was indicated at appraisal.

In three of the projects where co-financing was confirmed, the EBRD was the co-financing IFI and was identified at approval stage. All three projects were public sector transport infrastructure projects.

Co-financing with EU Pre-Accession Instruments

There are 14 projects in the sample of 43 with some evidence of co-financing by PHARE, ISPA and, in one case, the EU Solidarity Fund. There are six further cases of EU instrument activity for related projects.

Of the 13 project examined in depth, four (just under a third) were co-funded with EU grant instruments. This broadly mirrors the proportion found in examining the extended sample. Of these, the extent of cooperation was generally confined to the partitioning of the project and the division of labour between the two institutions. The EIB tended to lead during appraisal and ISPA during monitoring but with no real cooperation during either phase. In project 7 the Bank left all monitoring to ISPA but did not appear to receive any of the reports and part of the Banks project was not covered by the PIU. In project 1 ISPA insisted on a 10 year maintenance plan for its road components but the Bank made no special provision. In project 9 the impression was formed that the Bank financed those parts of the road network which ISPA was not interested in. The relationship can only really be described as parallel financing under these circumstances.

When compared with levels of co-financing within the EU, one third of projects could be considered as a relatively high level of cooperation. However, given common priorities, lower lending volumes and the more limited project pipeline opportunities during the pre-accession period there would appear to be scope to have improved cooperation.

Other Cooperation

The extent to which cooperation took place at country and sector level is more difficult to establish independently as this is not recorded in project files. There are indications that cooperation in the water sector in particular was more developed than in other sectors. However, if the overall results are examined, the under representation of certain sectors in the portfolio and the presence of unresolved sectoral issues on several of the projects examined in detail tend to suggest that cooperation at country and sectoral level needs to be strengthened.

7.5 CONCLUSIONS

At a project level the Bank's operations had a positive impact on the accession process. The great majority of projects were rated satisfactory or better, and this proportion showed an improvement over the older projects examined as part of the evaluation. Even those projects which exhibited unsatisfactory aspects made positive contributions in other areas.

At a sector and country level, the Bank's positive impact was limited by a number of operational and practical constraints. Considerable long term efforts would be required to overcome these difficulties, and whilst there is some evidence that the Bank was prepared to adapt its approach to the extent necessary to tackle certain sectoral problems, this more pro active approach was not universal and in general did not attain the level of concerted national and international cooperation which would be required to make a significant impact on constraints at supra project level.

Given that in most cases the attractiveness of the Bank's funds gave it significant influence during the pre-accession process, it could be argued, particularly if it were to have acted in concert with other IFIs and the Commission, that the Bank should have done more to develop sectors and institutions which would in the longer term have increased the pipeline of bankable projects and allowed it to further improve the alignment of its activities with EU priorities.

EVOLVING FRAMEWORK FOR LENDING PRIOR TO ACCESSION

ACCESSION TIMETABLE FOR THE TWELVE NEW MEMBER STATES

According to Article 49 of the Treaty on European Union, any European country may apply for membership if it respects the principles of liberty, democracy, respect for human rights and fundamental freedoms, and the rule of law - principles which are common to the Member States. Accession can only follow if the given European country fulfils all the criteria of accession which were fixed by the European Council in Copenhagen in 1993, reinforced by the Council in Madrid in 1995 and which subsequently became known as the '**Copenhagen Criteria**'.

- stable institutions guaranteeing democracy, the rule of law, human rights and respect for protection of minorities;
- a functioning market economy and the capacity to cope with competition and market forces in the EU;
- the capacity to take on the obligations of membership, including adherence to the objectives of political, economic and monetary union;
- adoption of the acquis communautaire (the entire European legislation) and its effective implementation through appropriate administrative and judicial structures.

Furthermore, the EU must be able to absorb new members, so it reserves the right to decide when it will be ready to adopt them.

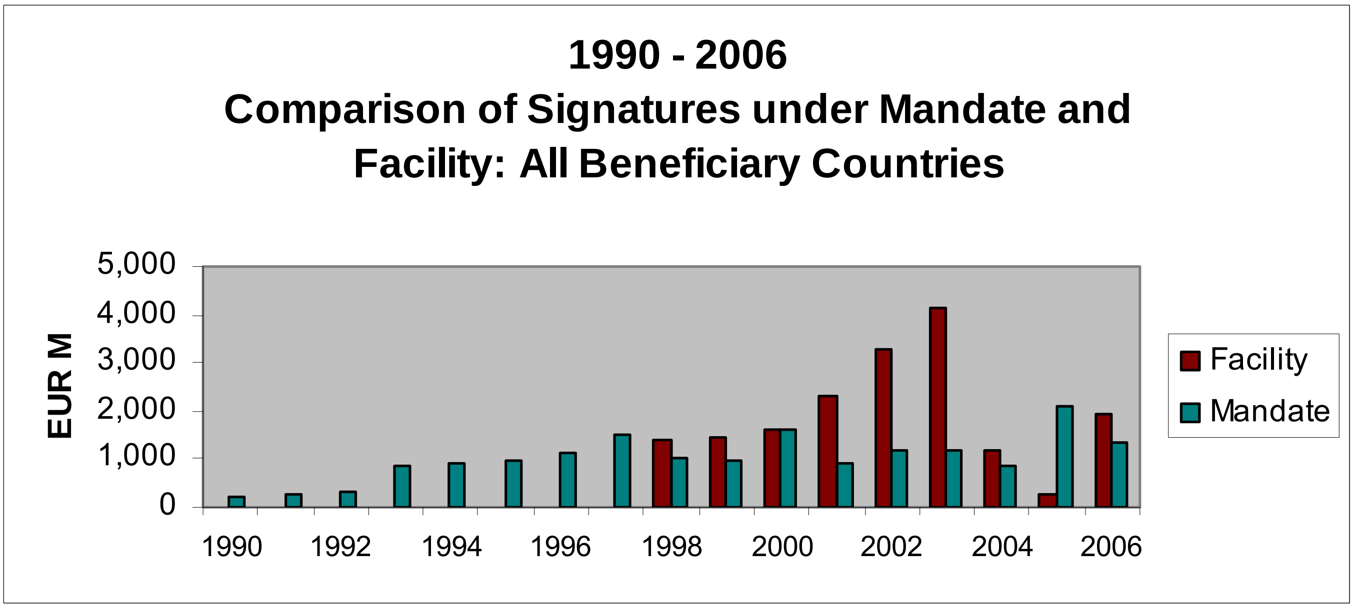
In 1990, Cyprus and Malta applied for membership of the EU. Malta renewed its application in 1998.

In 1994, Hungary and Poland applied for membership of the EU. In 1995, Romania, Slovakia, Latvia, Estonia, Lithuania and Bulgaria applied for EU membership. In 1996, the Czech Republic and Slovenia applied for membership of the EU.

On 31 March 1998, accession negotiations were commenced with, inter alia, Hungary, Poland, Estonia, the Czech Republic, Slovenia and Cyprus. In February 2000, accession negotiations were commenced with Romania, Bulgaria, Slovakia, Latvia, Lithuania and Malta. All accession negotiations were concluded in 2002.

The Treaties of Accession for Poland, Hungary, the Czech Republic, Slovakia, Slovenia, Estonia, Latvia, Lithuania, Cyprus and Malta were signed in Athens on 16 April 2003. These ten countries became Member States of the EU on 1 May 2004.

The Treaties of Accession for Bulgaria and Romania were signed in Luxembourg on 25 April 2005. These countries became Member States of the EU on 1 January 2007.



First Mandate 1990-1993

In October 1989, the Council invited the Bank to make loans available in Poland and Hungary and, on 29 November 1989, the Bank's Board of Governors authorised the Bank to grant loans in these two countries up to a ceiling of EUR 1bn subject to receipt of a full Community guarantee. The 100% Guarantee from the Community Budget was given by the Council to the Bank in February 1990, giving full coverage against any losses incurred in Poland and Hungary[23]. A Guarantee Agreement between the European Communities and the EIB was signed in April/May 1990.

On 25 February 1991, the Council extended the 100% Community Guarantee by EUR 700m to cover operations in the Czech and Slovak Republics, Bulgaria and Romania. On 27 February 1991, the Council invited the Bank to lend under own resources in these countries and this was authorised by the Bank's Board of Governors on 18 April 1991.

Council Decision 93/166 of 15 March 1993 granted the EIB a three-year 100% guarantee of EUR 200m for operations in the three Baltic States. On 22 March 1993, the Council invited the Bank to make loans to the three countries and this was authorised by the Bank's Board of Governors on 13 July 1993.

In June 1993, the Copenhagen Council agreed that the associated countries in Central and Eastern Europe that so desired should become members of the EU.

[23] A communication by the Commission, SEC (89) 1643 Final of October 1989 stated that tentative estimates of EIB lending in both countries over the following three years would amount to EUR 800-EUR 1 000M and that the Community Budget Guarantee should cover this amount.

Second Mandate 1994-1997

Council decision 93/696/EC of 13 December 1993 granted a 100% guarantee for three years for a ceiling amount of EUR 3bn for operations in Poland, Hungary, the Czech Republic, Slovakia, Romania, Bulgaria, Estonia, Latvia, Lithuania and Albania[24]. According to the terms of this decision, all future Bank operations in these countries were to be accorded uniform treatment within an overall framework. The amount proposed was based on the Commission's estimate of current annual EIB lending in these countries and the emphasis to be given to TENs. There were no specific limits for individual countries. On 24 January 1994, the Council invited the EIB to continue its operations in these countries, and this was authorised by the Bank's Board of Governors on 2 May 1994. At this time, the EIB was already under pressure to reduce its reliance on the 100% Community Guarantee.

Third Mandate and First Pre-Accession Facility 1997-2000

Mandate

On 14 April 1997, via Decision 97/256/EC, the Council of the European Union granted a Community Guarantee to EIB against losses under loans for projects in Central and Eastern Europe: Albania, Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia and Slovenia. The guarantee, amounting to ECU 3,520 million for three years from 31 January 1997 to 31 January 2000, was restricted to 70% of the aggregate amount of the credits opened, plus all related sums. The EIB was also invited to aim to cover the commercial risk on 25% of its lending from non-sovereign guarantees. The ceiling of the new Mandate for CEEC was agreed by the Council on the understanding that a substantial pre-accession support facility would be established by the Bank in late 1997. According to the Council of December 1996, "The volume of external lending shall respect the Financial Perspective and Community Budget Discipline as well as the EIB internal guidelines on lending to third countries and take into account the conclusions of the European Councils at Essen, Cannes and Madrid. The approach of a blanket guarantee, without distinguishing regions and projects, is approved. A risk-sharing element as proposed by the Commission and the EIB is accepted."

Pre-Accession Facility

On 14 April 1997, the Council of the European Union invited EIB to create a substantial Pre-Accession support Facility to be approved under the second paragraph of Article 18 of the Bank's Statute. This Facility would not be covered by any Guarantee from either the Community Budget or the Member States. It was stated at the time that the invitation from the Council to establish the Facility met the unanimous agreement of the Member States and of the Commission, and facilitated the agreement on the ceilings for the various geographical areas (ALA, MED, CEEC) confirmed by the Governors in June 1997.

According to the Board of Governors' Decision of 26 January 1998 establishing this Pre-Accession Facility, its purpose was *to facilitate and accelerate progress in all sectors normally eligible for EIB financing, notably in areas of key European Union policy objectives. Emphasis was to be given to integration projects and those facilitating the adoption of the acquis communautaire (with particular emphasis on environmental protection) in areas like the development of transport, telecommunication and energy links (TENs), the development of industrial competitiveness and regional development.* It was decided that the Facility of EUR 3.5bn would run concurrently with the CEEC Mandate of EUR 3.52bn up to 31 January 2000. The amount was based on the Community mandate ceilings for the CEEC region. Lending, at the Bank's own risk, was not to be subject to the 10% guideline for lending to third countries in view of the transitory character of the pre-accession period. The amount was to double the existing mandate and was estimated to be sufficient to cover the Bank's reinforced pre-accession action in favour of all applicant countries during the said period. The overall amount reflected the needs and absorption capacity of the countries concerned as well as the capacity of the Bank.

[24] (Mandate PECO 2.5.1994)

The Facility was open to all applicant countries and Cyprus on the understanding that sovereign loans to sub-investment–grade countries would continue to be under the lending Mandate rather than under the Facility. Lending to Governments or taking political risk in commercial operations should be acceptable to the Bank in investment grade countries. Countries closer to accession could benefit more from the Facility, and the Mandate could be made available for weaker applicant countries. Loans already approved by the Board could be transferred to the Facility with Board approval (sovereign operations in key countries), and it was estimated that some EUR 1bn of loans could qualify for transfer to the Facility. The main purpose of the transfer was to ensure that sufficient room would remain available under the Mandate in order to satisfy the financing needs and strengthen as much as appropriate the Bank's support to the weaker applicant countries, thus helping to reduce gaps and avoid discrimination. The Bank would continue to apply its project-based approach, taking full account of the priorities adopted by the Council in the Accession Partnership Agreements

The choice between Mandate or Facility would be dealt with flexibly, on a case by case basis, under a judicious modulation that would take account of the relevant country situation, the project nature, the characteristics of the financing proposed, and the available securities.

Fourth Mandate (2000-2007) and Second Pre-Accession Facility (2000 – 2010)
Mandate
By decision 2000/24/EC of 22 December 1999, the Council gave a 65% global guarantee to EIB loans for a ceiling amount of EUR 8.68bn in the countries of Central and Eastern Europe: Albania, Bosnia & Herzegovina, Bulgaria, Czech Republic, Estonia, Macedonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia and Slovenia. Bank documentation stated that the reduction in guarantee coverage from 70% to 65% stemmed primarily from the budgetary provisioning of the Guarantee Fund. The guarantee was to last from 1 February 2000 to 31 January 2007. It was stated in the decision that, where the commercial risks are adequately covered by non-sovereign third parties, the guarantee of the Community would be restricted to political risks, namely the risk of non-transfer of currency, expropriation, war or civil disturbance. Furthermore, the Bank was invited to cover the commercial risk on 30% of its lending with non-sovereign guarantees as far as possible on a regional mandate basis, this percentage being increased whenever possible, insofar as the market permits. On 22 December 2004, in decision 2005/47/EC, the Council decided that the Community guarantee in risk-sharing operations is extended to cover a further category of political risk, namely denial of justice upon breach of certain contracts by the Host Government. Furthermore, the Bank should secure under the risk-sharing scheme commercial risks by means of non-sovereign third-party guarantees or by means of any other security or collateral as well as by relying on the financial strength of the debtor, in accordance with its usual criteria.

The Copenhagen Council of December 2002 concluded that pre-accession support for Turkey would be financed from 2004 under the budget heading Pre-Accession Expenditure.

On 22 December 2004, in decision 2005/47/EC the Council amended decision 2000/24/EC and restructured the old CEEC Mandate into a South-Eastern Neighbours Mandate, excluding the eight new Member States which acceded to the EU on 1 May 2004, but still including Turkey. The revised ceiling was EUR 9 19bn for South-Eastern Neighbours: Albania, Bosnia and Herzegovina, Bulgaria, Croatia, FYROM, Romania, Serbia and Montenegro, and Turkey. All credits previously opened for projects in the CEEC and Turkey mandates were to be deducted from this amount. A restated and amended Guarantee Agreement was signed on 3 August and 2 September 2005

Pre-Accession Facility II

On 4 January 2000, the Bank's Board of Governors established the second Pre-Accession Facility of EUR 8.5bn for the initial 3.5 years from 2000 to 4 July 2003. The Facility was open to all applicant countries plus Cyprus and Malta. The Facility was entirely at the Bank's own risk and was not subject to 10% lending limit outside the Community. The initial timescale was decided in order to coincide with the mid-term review of the EU financial perspectives in mid-2003 and would be under progressive review. The amount decided was based on EIB activity, the sectors eligible for financing and their economic needs, the amount envisaged under Mandate, the economic growth of the countries concerned and their commitment towards EU membership.

Loans under the Facility were to be used to facilitate and accelerate progress in all sectors normally eligible for EIB financing, notably in areas of key EU policy such as transport infrastructure, energy and telecommunications, environment and municipal investments, SMEs and industry, and when possible and appropriate, investments in human capital (e.g. health and education). Close attention was to be given to integration projects as well as projects that foster regional development, promote industrial competitiveness and contribute to the creation or safeguarding of employment.

In April 2001, the Board of Governors authorised the Bank to grant Turkey loans under the Per-Accession facility.

On 4 June 2003, the Bank's Governors' decided to increase the Facility by a further EUR 3.5bn until end-2004, thereby establishing a new ceiling of EUR 12bn for this Facility. This was because the initial period and indicative level of activity were no longer sufficient to allow completion of the Bank's forecast lending programme under the Facility. The decision also indicated that, post-enlargement, a new proposal should be put forward to cover lending in those countries not in the first round of accession.

On 14 May 2004, the Bank's Governors' increased the Facility by a further EUR 2bn until end-2006 for those countries not included in the first accession round. Furthermore, it was necessary to avoid an interruption of lending activity in 2004, even before accession, as signatures at the time were forecast to exceed the ceiling of EUR 12bn. All candidate countries, as well as Acceding and Accession States were to be eligible for lending under the Pre-Accession facility.

A new proposal for a Pre-Accession Facility was to be brought forward when the EU had decided on the new Financial Perspectives.

EUROPEAN INVESTMENT BANK
OPERATIONS EVALUATION (EV)

In 1995, Operations Evaluation (EV) was established with the aim of undertaking ex-post evaluations both inside and outside the Union.

Within EV, evaluation is carried out according to established international practice, and takes account of the generally accepted criteria of relevance, efficacy, efficiency and sustainability. EV makes recommendations based on its findings from ex-post evaluation. The lessons learned should improve operational performance, accountability and transparency.

Each evaluation involves an in-depth evaluation of selected investments, the findings of which are then summarized in a synthesis report.
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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)).
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