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# Synthesis Report

## Evaluation of Special Dedicated Global Loans in the European Union between 2005 and 2007

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**SYNTHESIS REPORT**

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**NOTICE**

**The EIB has an obligation of confidentiality to the owners and operators of the operations 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

| | |
|---|---|
| Allocation | A single loan provided by a FI to a FB and presented for approval to the Bank as part of the justification process for funds already disbursed, or to be disbursed, by the EIB. |
| Allocation Procedure | The control mechanism designed to ensure that disbursed funds have been used for the intended purpose. |
| Article 267 | Article of the "Consolidated Version of the Treaty Establishing the European Community" which defines eligible areas of involvement for the EIB. |
| Asset Backed Securities | Asset Backed Securities (ABS) are issued by a segregated SPV and are backed by a pool of assets originated by a bank or another institution, known as the originator. Securitised assets are fully transferred to an SPV via a true sale or synthetically by means of a credit default swap (or any other form of synthetic risk transfer techniques). The SPV is bankruptcy remote from the originator itself. For payments of interest and principal, ABS notes rely on cash flows deriving from the securitised assets or, in the case of synthetic securitisations, from the collateral and the credit default swap premia. |
| BPs/bps | Basis Points, 1 bp = 0.01% of interest |
| COP | Corporate Operational Plan |
| Covered Bonds | Covered Bonds constitute a senior secured debt obligation of the issuer with recourse to a cover pool of high quality mortgages or public sector assets. The cover pool acts as collateral in the case of the issuer's insolvency - hence the name "covered bonds". In the case of Structured Public Sector Bonds, the issuer is a public sector entity, whilst for covered bonds, the issuer is typically a bank, a financial institution or a specialised dedicated entity. Although some sort of ring-fencing can be put in place in order to guarantee first recourse of the Note holder to the underlying pool of assets, there is no segregation between the Notes and the issuer itself (i.e. if the latter defaults, the Notes will default through the cross default clause). |
| Disbursement | Tranche of funding supplied to a Borrower |
| EIB (the Bank) | European Investment Bank |
| EV | Operations Evaluation of the EIB |
| FI | Financial Intermediary |
| FB | Final Beneficiaries of the Global Loan |
| GL | Global Loan |
| Loan Substitute | Loan Substitutes ("LS") are an alternative means of providing funds to a project promoter or intermediary. Instead of disbursing funds via a loan, the Bank subscribes a Note issued by a Special Purpose Vehicle (SPV) or by the intermediary itself, which in turn channels the funds and the financial advantage provided by the EIB to the final beneficiary. By deploying capital market instruments, such as covered bonds and ABS as a substitute for loans, the Bank significantly increases its ability to diversify the nature of its lending activity. |
| NPL | Non Performing Loan |
| Objective Area | Objective 1 and Objective 2 regions, often called "assisted areas" or "less developed regions", are defined by the EC on the basis of macro-economic criteria (per capita GDP, measured in purchasing power parities, of less than 75% of the Community average for Objective 1 regions; unemployment rate, loss of industrial employment, population, etc for Objective 2 regions) or on the basis of geographical or demographic characteristics (peripheral regions, regions with low population density). |
| On lending | The lending by the FI to the FB, when the FI is in receipt of EIB funding. |

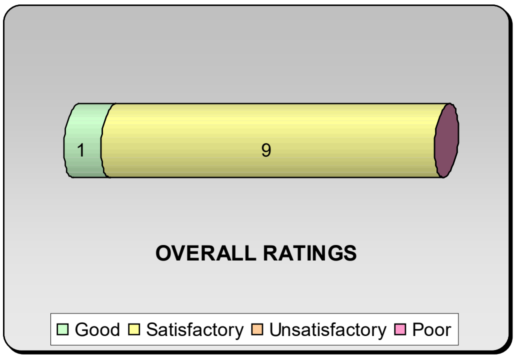
## EXECUTIVE SUMMARY

This report represents the synthesis of an evaluation carried out by EV of the EIB financing of smaller projects and enterprises through lines of credit within the EU where the majority of the final beneficiary projects are dedicated to specific EIB objectives (Dedicated Global Loans). The evaluation concentrates only on those operations which are dedicated to other than, or something in addition to, SMEs – henceforth referred to in this report as Special Dedicated Global Loans.

Ten individual Special Dedicated Global Loan operations have been examined out of a portfolio of 154 operations signed between 2005 and 2007 in 21 different countries for a total (signed) value of EUR 16.5 billion. Germany was the main beneficiary both in terms of number of operations (32) and total amount signed (EUR 4.9 billion).

### Overall Performance

All ten of the operations examined were fully disbursed and allocated and were rated as Satisfactory (or better in one case). In particular there was clear evidence that the EIB core objectives targeted through the dedication of the operation had been achieved and in some cases exceeded. The Bank had shown considerable flexibility in its requirements to suit individual operations and Financial Intermediaries and relationships were uniformly good, with repeat business being an important aspect of this type of operation. In most cases the Bank's added value was not significant, but there was no evidence of a lack of demand for the line of credit product.




### Relevance of Operations

All operations addressed one or more of the Bank's core objectives, with nine out of ten addressing more than one. In this case the Bank's core objectives are also well aligned with EU and country priorities.

### Operation Performance

The FIs were able to show that the Bank's funds were used for eligible investments and in accordance with additional conditions used to encourage increased term lending to SME's or investments in particular dedicated objectives (notably Objectives 1 and Objectives 2 areas). All operations achieved the dedicated objectives set at appraisal. In most cases the allocated portfolio exceeded the 70% level of dedication targeted at appraisal and in addition contained significant portions which met other core EIB objectives – notably lending to SMEs. A more detailed breakdown of ex post dedications is given in Appendix 1.

All of the operations analysed were fully disbursed and allocated. A few required an extension period to allow the funds to be disbursed, but the extension was never significant and the operations were eventually allocated within acceptable time limits.

| Ex post vs ex ante dedication to COP objectives 2006-2008 | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| **Operation no** | **1** | **2** | **3** | **4** | **5** | **6** | **7** | **8** | **9** | **10** |
| **Economic and Social Cohesion in the enlarged EU** | • | • | □ ● | □ ● | □ ● | □ ● | □ ● | □ ● | □ ● | □ ● |
| **Innovation 2010 Initiative (i2i)** | □ ● | □ 47% | □ ● | | | • | • | • | • | • |
| **Development of Trans-European and Access Networks** | | | • | • | | ● | • | | • | • |
| **SMEs or Micro** | | | □ ● | □ ● | ● | | | □ ● | | □ ● |
| **Environmental Sustainability** | | □ 52% | • | | | • | • | • | • | |

□ ex-ante dedication (>70%)

● ex-post contribution to COP objecitves (>70%)

• ex-post contribution to COP objectives (between 20% and 70%)

Please note that:
(i) COP refers to Corporate Operational Plan 2006-2008 of the EIB.
(ii) For operation 2 the ex-ante dedication was min 70% i2i or Environment.

### Financial Intermediary Performance

Eight operations were rated Good. Most of these were repeat operations and the Financial Intermediaries had shown on many occasions during previous years their capability to implement EIB's objectives successfully. One operation was considered to be below expectations, largely due to financial distress faced by the Financial Intermediary at the time of the appraisal - but having improved since then.

The awareness by Financial Intermediaries of EIB's environmental and social standards was rated Satisfactory or better in all cases. Indeed in two cases the FI demonstrated its capacity not only to manage operations in compliance with EU and/or national regulations but also to develop a proactive environmental approach.

### Sustainability

All the Financial Intermediaries were sustainable, supported by a good standing with the Bank and the various rating agencies. The low perceived level of banking sector risk in the countries in which the Global Loans were implemented, together with the essential contribution of the FIs to the banking sector either at national or regional level, indicated a sustainable business in all cases. The level of non-performing loans was uneven throughout the sample, but all FIs had satisfactory levels of credit losses, consistently below the average of the country or sector peers.

### EIB Contribution

The Special Dedicated Global Loans facilitated the Financial Intermediaries' continued presence in the very competitive public sector and SMEs loan markets and enabled the Final Beneficiaries to achieve lower funding costs and longer tenors than otherwise. However, transparent processes were not always in place and therefore it was difficult to quantitatively determine the degree to which the EIB financial advantages were being passed on to the Final Beneficiaries. The institutional and technical contribution of the EIB was not significant in most cases.

### EIB Management of Operation Cycle

The Bank had good and long established relationships with most of the Financial Intermediaries and the appraisal was well structured. Although the overall Bank's performance on operation-cycle management is considered Satisfactory for the operations evaluated, certain weaknesses were noticeable, particularly in the quality of monitoring and reporting activities.

## TABLE OF RECOMMENDATIONS

| | Observations & Recommendations | Reponses of Operational Directorates |
|---|---|---|
| | **Observation:** All ten of the operations examined were fully disbursed and allocated and were rated as Satisfactory (or better in one case). In particular there was clear evidence that the EIB core objectives targeted through the Dedication of the operation had been achieved and in some cases exceeded. The Bank had shown considerable flexibility in its requirements to suit individual operations and Financial Intermediaries and relationships were uniformly good, with repeat business being an important aspect of this type of operation. In most cases the Bank's added value was not significant, but there was no evidence of a lack of demand for lines of credit. On the contrary, the Bank itself limits the volumes for this type of operation. Relative deficiencies identified were minor and were related to the administration and documentation of these operations (see recommendations below.) | **Whilst welcoming the overall positive assessment of the Dedicated Global Loans product, two points should be recognised: firstly, there are many factors that contribute to the value added of an operation, including diversification of funding; intermediaries also provide a conservative feedback on the Bank's financial value in order to maintain their negotiation margin for future EIB operations.**<br>**Secondly throughout the period of the evaluation, the internal IT applications have already been significantly enhanced for global loans.** |
| <br><br><br><br><br><br><br><br><br><br>1<br><br><br>2a<br><br><br><br><br>2b<br><br><br><br><br><br>2c<br><br><br>3<br><br>4 | **Recommendation:** The Bank should review its documentation requirements for Global loans with a view to on the one hand streamlining the process, and on the other hand collecting additional key data. It is recognised that many of these issues have already been addressed in the new Global Loan for SMEs product, although it is too soon to draw any conclusions on the practical implications of the new product for systematic documentation. However, changes should incorporate the following elements:<br><br>• Information requirements should be standardised and should include data on maturity, interest rates, currency, prepayments and non-performing loans.<br>• The practice of reporting on the ex ante allocation of previous GLs during the approval of subsequent operations should be replaced with a regular and standardised reporting procedure for all GL operations containing current allocation information.<br>• Better use should be made of the Bank's existing electronic tools to record systematically, on a cross directorate basis, key post signature operational activity. This will facilitate dissemination of operational information and assist in the handover of operations to new staff.<br>• The annual management report on global loans should be reinstated, based on improved data capture to facilitate the process.<br>• The Bank should examine a reasonable sample of Final Beneficiaries ex post.<br>• The process of transferring allocation information should as far as possible be automated to avoid manual transcription. | **It must be recognised that observations made by EV have been addressed by the revised Loans for SME's product.**<br>**Similar progress is in course for Global Loans dedicated to municipalities and local authorities, where the objectives of increased transparency and transfer of benefit to the final beneficiary must be pursued whilst taking account of market constraints specific to public lending (narrow financial margins, competitive bidding).**<br>**1. The documentation process for Loans for SMEs is the result of substantial streamlining of the former process and establishes a set of standard indicators to be provided by all intermediaries, including the name, address and NACE code of the final beneficiary; number of employees; loan/lease amount granted by the intermediary; allocation amount; duration of the loan; and financial advantage transferred in basis points; method of transfer of financial benefit. Documentation requirements also take account of differences in the availability of information between EU-27, Candidate and Potential Candidate Countries and Eastern Partner Countries. Reporting requirements in relation to global loans and loans for SMEs secured by Multiple Assignments of Rights were further strengthened.**<br>**2. Information in relation to allocations under loans for SMEs is provided at the end of the allocation period. As defined in the Finance Contract, the intermediary must submit to the Bank** |

an Allocation List summarising information on the loans granted to SMEs to justify utilisation of the funds. In addition the Intermediary is encouraged to provide regular interim Allocation Lists to give more frequent feedback to the Bank on the utilisation of the Loan to SMEs. The Bank's existing electronic tools have been continuously improved since their implementation and now contain a significant volume of information pertaining to both GL and Loans for SME's; this information is collected on a cross-directorate basis. The former annual management report on Global Loans, produced by the Projects Directorate, has been replaced by the requirement to include, in the Board Reports of Loans for SMEs, details on the Bank's SME lending activity in the country concerned over the past three years. This approach allows to provide more timely information on the Bank's SME lending activities in relevant geographical areas.

3. Under its loans for SMEs the Bank may also carry out more detailed studies of a representative sample of sub-loans in order to verify the accurateness of information received from the intermediary.

4. The process by which allocations are treated is continuously being improved through the use of standard format files, in line with the information requirements. These are automatically uploaded and manual intervention is generally in the case of exceptions to the upload process. It should be highlighted that the first tools of this type became available after many of the operation in this study were allocated. Generally speaking manual intervention should be considered the exception and not the rule.

# 1. Introduction

This report represents the synthesis of an evaluation carried out by EV of the EIB financing of smaller projects and enterprises through lines of credit within the EU where the majority of the final beneficiary projects are dedicated to specific EIB objectives (Dedicated Global Loans). The evaluation concentrates only on those operations which are dedicated to other than, or something in addition to, SMEs – henceforth referred to in this report as Special Dedicated Global Loans.

The evaluation is primarily intended to assist the EIB's governing bodies in the formulation of Bank policy and strategies. It will also offer practical support to the operational departments of the Bank. Outside the EIB, the evaluation may also be of interest to the general public, including public authorities and private sector promoters.

## 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 considered. This evaluation report is a synthesis of the findings of the individual evaluations. The work was carried out by external consultants (PricewaterhouseCoopers Luxembourg) and supervised by EV staff.

In accordance with the Bank's evaluation procedures, individual operations were rated in four categories: "Good", "Satisfactory", "Unsatisfactory" and "Poor"[1]. The evaluation assesses each of the operations using the following OECD/DAC criteria: Relevance, Effectiveness, Efficiency, and Sustainability. In addition, a special rating is given for Environmental and Social performance.

The EIB contribution is also assessed, taking into consideration the financial contribution to the beneficiaries, as well as the non-financial contribution through transfer of expertise, technical assistance or any other form of support. It also includes an assessment of the cooperation with other funders, where appropriate. In addition, the management of the operation cycle by the Bank is assessed.

*Sample Selection process:*

This evaluation covers ten line of credit operations (Global Loans or GLs) financed by the EIB from own resources signed during the 2005-2007 period and which were dedicated to a core EIB objective other than, or in addition to, SMEs. The selected operations were drawn from the 56 operations which (i) had been disbursed for at least 70% and (ii) allocated for at least 50% of the total loan amount signed. The selection aims at providing a cross section which is as representative as possible of the portfolio distribution in terms of sector, country, size, dedication and allocation procedure. In selecting the operations, EV has excluded those with FIs that have been visited in recent evaluations.

Detailed operation analysis and field visits have been conducted for the selected operations, including a selection of visits to Final Beneficiaries (FBs). Individual evaluation reports have been prepared and discussed with the operational staff associated with the operation, and the main elements will be provided to operation promoters for their comments. As usual, the information contained in these reports is of a confidential nature and availability is restricted.

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

The following table summarises the main features of the selected operations.

| Operation | Country | Signed amount (€ m) | Dedication |
|---|---|---|---|
| 1 | Germany | 100 | Financing small and medium sized projects promoted by the public sector in Germany and contributing towards the EIB's innovation 2010 initiative and focussing on education and training, research and development. |
| 2 | Germany | 300 | Financing small-scale eligible investments in Germany that contribute toward the EIB's innovation 2010 initiative and the fields of environment or health |
| 3 | Germany | 40 | Financing small scale public and private investments in human capital and social housing in Brandenburg, an EU convergence region |
| 4 | Spain | 100 | Financing regional development and/or common interest projects of limited scale promoted by SMEs (70%) and local authorities |
| 5 | Spain | 90 | Financing regional development and/or common interest projects of limited scale promoted by SMEs (70%) and local authorities |
| 6 | Italy | 200 | Financing project of small and medium-scale infrastructure schemes in regional development areas |
| 7 | France | 300 | Financing project of small and medium-scale infrastructure schemes in regional development areas |
| 8 | Portugal | 150 | Financing SMEs in the development of their businesses, contributing to competitiveness and productivity and covering mostly Convergence areas |
| 9 | Austria | 100 | Financing small and medium sized projects in regional development areas in Austria and other EU member states |
| 10 | Poland | 50+28 | Financing SMEs in the development of their businesses, contributing to competitiveness and productivity and covering mostly development regions |

## 2. Background

In its role of provider of long-term funding for projects which foster the interests and policies of the EU, the EIB has since its earliest operations adopted a mechanism to fund small scale investments which were too small for EIB direct lending. Global Loans are open lines of credit to Financial Intermediaries (FIs), which in turn provide an equivalent amount of funding to their smaller clients. The FIs on-lend the proceeds, at their own risk, to finance small and medium scale projects - either ventures mounted by SMEs or small-scale infrastructure schemes.

The Bank's objectives for Global Loans were reviewed in 2000, when, for the sake of transparency, the majority of Global Loans began to be targeted (in other words dedicated) to a specific pre-defined objective that was one of the operational priorities set out in the Bank's COP. The concept of Dedicated Global Loans has since become the norm, but "mixed" (those that can fund both SMEs and small infrastructure ventures promoted by public sector authorities) and/or "multi-purpose" GLs may be approved on an exceptional basis (typically very small economies that may not have a large enough customer base for specialisation or for regional financial intermediaries or risky environments that require lending of shorter duration). A GL is classified as being Dedicated if at least 70% of allocations target one particular objective as prescribed in the COP (convergence, SMEs, i2i, environmental protection, etc.).

The evolution of the Dedicated GLs during recent years is presented in the following table based on the Bank's annual global loan reports[2], and illustrates the gradual shift away from small scale infrastructure to Regional Development and SME lending. In 2006, the volume of Global Loan signatures (EUR 11 billion) represented more than a quarter of total Bank's lending activity by volume (27% in EU-27 and 29% in EU-15).

[2] Annual reports for 2007 and 2008 were not available, as the practice of reporting annually on global loans was discontinued.

| Number of GLs associated to the COP Objectives | 2002 | 2003 (EU) | 2004 | 2005 | 2006 |
|---|---|---|---|---|---|
| Regional Development | 11 | 9 | 22 | 25 | 50 |
| Reg. Dev. - SME | 9 | 25 | 22 | 14 | - |
| Reg. Dev. - i2i | - | - | - | 4 | - |
| Reg. Dev. - Small-scale Infra. | 10 | 16 | - | - | - |
| Reg. Dev. - Environment | 1 | - | 3 | - | - |
| SME | 30 | 20 | 24 | 23 | 46 |
| SME - i2i | 2 | - | | | |
| i2i | 1 | - | 3 | 2 | 4 |
| Small-scale Infra. | 18 | 11 | - | - | - |
| Environment | 1 | - | - | - | 5 |
| SUB-TOTAL | 83 | 81 | 74 | 68 | 105 |
| Non-dedicated | 7 | 3 | 12 | 4 | 2 |
| **TOTAL** | **90** | **84** | **86** | **72** | **107** |

## 2.1. The EIB Global Loan mechanism

After the careful appraisal of appropriate counterparts, the EIB will grant a line of credit to a particular Financial Intermediary on condition that the FI allocate the funds to Final Beneficiaries which are active in the targeted policy area. The credit risk of the Final Beneficiaries remains with the Financial Intermediary, who also undertakes to manage the use of EIB funds in accordance with pre-set requirements.

The actual disbursement and allocation mechanism may vary, depending on the allocation procedure used and the previous experience with the FI:

- Dossier or Fiche: FIs submit a dossier regarding each individual allocation summarizing the essential information necessary for its economic, financial, technical and environmental appraisal. This approach is now less common inside the EU.
- Allocation by list (i.e. “List-based”): FIs draw up a list including, for each venture proposed, the essential information to permit its identification and to ascertain its compliance with the criteria laid down for the GL.
- Portfolio approach[3]: FIs report globally on the development, volume and structure of their overall portfolio.

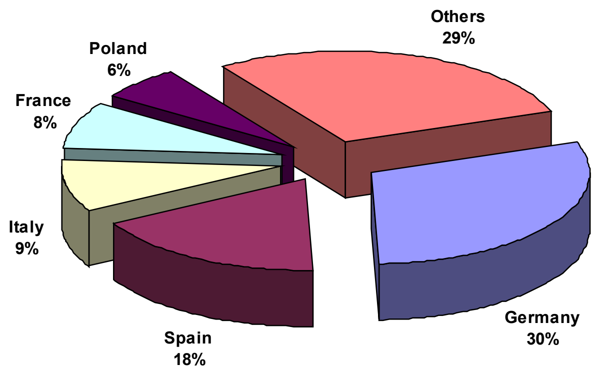
For an FI with a long established GL relationship, a typical procedure would involve a request by the FI for a disbursement of a tranche of funding, at a time it chooses. It then has a period of twelve to twenty-four months to provide allocation data that can satisfy the Bank that the funds have been used appropriately.

## 2.2. Presentation of the EIB Special Dedicated Global Loans Portfolio 2005-2007

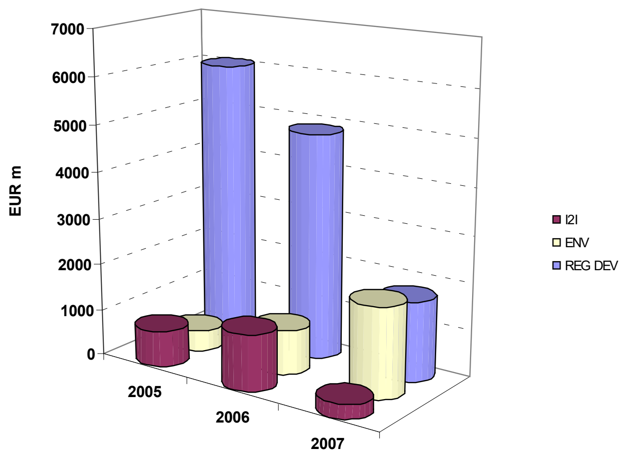
During the period 2005-2007, the Bank signed 230 GLs in 24 Member States for a total value of EUR 27.5 billion. Based on the information available, 120 Global Loans (46% of the total volume signed) targeted SMEs and 76 of them were solely dedicated to this objective. (It should be noted that GLs can target more than one objective.)

The present evaluation concentrates only on those Global Loans which were dedicated to other than, or something in addition to, SMEs. For the purposes of this evaluation these will be referred to as Special Dedicated Global Loans. These include 154 operations in 21 different countries for a total (signed) value of EUR 16.5 billion. Germany was the main beneficiary both in terms of number of operations (32) and total amount signed (EUR 4.9 billion) followed by Spain with 22 operations and EUR 2.9 billion in signatures, followed, in terms of number of operations, by Poland (16) and Austria (10) - but in terms of amount signed by Italy (EUR 1.5 billion), France (EUR 1.4 billion) and Poland (EUR 1 billion).

[3] The portfolio approach has no longer been available at the EIB since September 2008 for new global loans




The majority of the Special Dedicated Global Loans signed between 2005 and 2007 were channelled towards regional development areas (52% of the total volume signed), 9% of the total amount signed was dedicated to environment and over 7% of the total amount signed was dedicated to i2i. No operations were dedicated to the other COP objectives (Trans-European and Networks and Human Capital). The following graph shows the signature amounts during the three year period. It should be noted that, since GLs can be dedicated to more than one objective, the total amount dedicated does not equal the total amount signed.




The average amount signed per operation was EUR 107 million, ranging from EUR 15 million (four operations in New Member States) to EUR 400 million (two operations in France).

# 3. Policies & Strategies - Relevance

## 3.1. EIB Policies and objectives

All Global Loans reviewed were consistent with one or more of the operational lending priorities set out in the Bank's COP 2006-2008[4]:

- Economic and Social Cohesion in the enlarged EU;
- Implementation of the Innovation 2010 Initiative i2i (RDI, ICT, Education and training);
- Development of Trans-European and Access Networks - TENs;
- Support for SMEs;
- Environmental sustainability.

[4] Source: Corporate Operational Plan 2006-2008, EIB, January 2006

## 3.2. EU/Country objectives

**Case Study – Project 1 (i2i projects of limited size in the education and training sectors in Germany)**

The operation provided financing for small and medium sized projects promoted by the public sector in Germany and contributed towards the European Investment Bank's (EIB) innovation 2010 initiative ("i2i"). It also focused on education, training and research and development. Projects were targeted mainly at the education sector (schools as well as universities), where infrastructure enhancement was increasingly a priority in Germany.

The evaluation found that the operation financed primarily public sector projects including further education and primary and secondary school renovations which, because of their nature and size, required long-term financing.

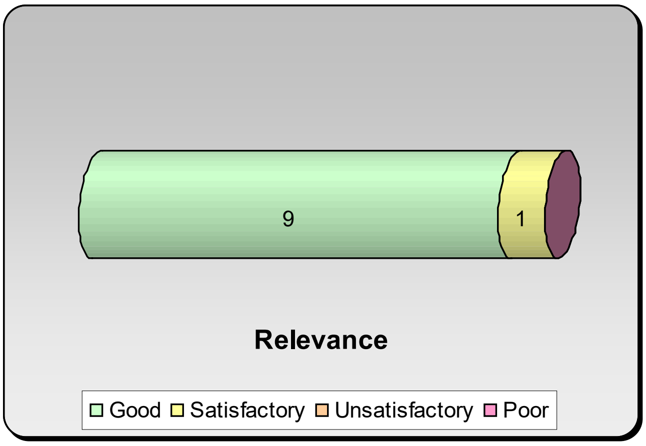
The operation continued the EIB's successful co-operation with one of the most important partners for financing of projects (mainly infrastructure) in Germany.

All selected operations were eligible under article 267 of the Treaty establishing the European Community and the EU Commission expressed its favourable opinion regarding the EIB participation in financing the projects covered under the operations in accordance with the Article 21 of the Bank's Statute. Moreover the operations contributed to the country objectives as noted in the Structural Funds and the Cohesion Policy specific to each country concerned.

## 3.3. Financial intermediary objectives

All selected Global Loans were in line with the Financial Intermediary objectives, either dedicated to public authorities or SMEs. Most of the Financial Intermediaries were among the oldest and most dynamic partners of EIB in the country concerned and this was regarded as evidence of the high capacity of the institution in implementing the EIB's objectives.

## 3.4. Relevance of Operations




*Relevance is the extent to which the operation objectives were consistent with EU policies, EIB objectives and the decisions of the EIB Governors, as well as the country policies. In the case of this evaluation relevance is more or less guaranteed by the process of dedicating operations to one or more of the Bank's core objectives. All operations therefore addressed one or more of the bank's core objectives, with 9 out of ten addressing more than one. In this case the Bank's core objectives were also well aligned with EU and country priorities.*

In one case (Operation 2), the EIB took the view that financing of school renovations was deemed to improve "access to quality education and training". It was noted during the evaluation that financing provided to meet the other two objectives (i.e. "supporting excellence in Research, Development and Innovation" and "promoting the diffusion of Information and communications technology (ICT) networks, including audiovisual activities") that define i2i was lacking when the loan allocations were analysed.

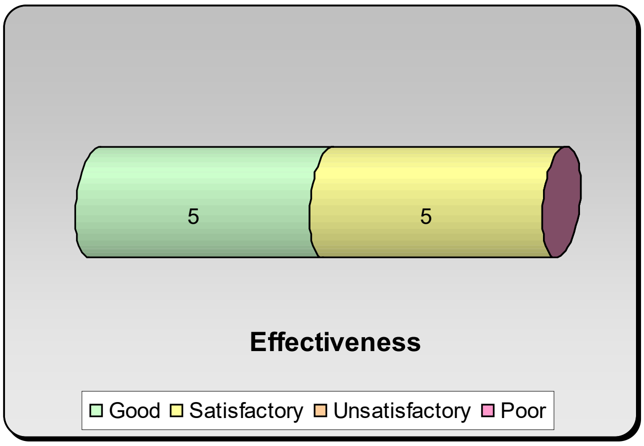
## 4. Operation Performance

The main purpose of the lines of credit (Global Loans) granted to Financial Intermediaries was to channel EIB funding to investments and Final Beneficiaries which were below the threshold for EIB direct lending – primarily to SMEs but also other financial intermediation operations such as microcredit and leasing. These operations are characterised by large numbers of smaller investments managed by a Financial Intermediary who accepts the credit risk of the Final Beneficiaries within his loan portfolio. The selection of strong Financial Intermediaries, with a sound organisation and management structure is an important feature of this type of operation since appraisal and monitoring of the financed sub-project is delegated to the Financial Intermediary.

This chapter follows the format of the standard operation performance assessment (quality of the operation) mirroring the Pillar 2 of EIB value added approach. The performance of lines of credit has been evaluated using standard EV criteria for these operations:

- Global Loan Performance (effectiveness);
- Financial Intermediary Performance (efficiency);
- Environmental and social performance;
- Sustainability.

### 4.1. Global Loans Performance (effectiveness)




*The effectiveness of the Global Loan is the extent to which the initial objectives of the loan with regard to amounts disbursed, targetted sectors, on-lending conditions and reporting, have been achieved.*

*All of the ten Special Dedicated Global Loan operations examined have been fully committed and achieved their overall objectives. This is a very positive assessment. In addition, five of the ten rated operations were considered to have exceeded expectations in a variety of ways.*

Operations were rated 'Good' except if one of the following observations or findings were noted: the FI has experienced a significant delay in the allocation (requiring an extension of the allocation period – operation 5), the final beneficiary visited was not informed of the EIB's involvement (operations 6 and 8), the corporate objectives and experience of the FI could not be fully substantiated (portfolio approach – operation 7).

#### 4.1.1. Allocations and Portfolio Characteristics

The FIs were able to show that the Bank's funds were used for eligible investments and in accordance with additional conditions used to encourage increased term lending to SME's or investments in particular dedicated objectives (notably Objectives 1 and Objectives 2 areas). All operations achieved the dedicated objectives set at appraisal. In one case (operation 2) the target dedication was to two objectives on an and/or basis. Including both objectives the operation was 99% allocated to core EIB objectives.

In most cases the allocated portfolio exceeded the 70% level of dedication targeted at appraisal, and in addition contained significant portions which met other core EIB objectives – notably lending to SMEs. A more detailed breakdown of ex post dedications is given in Appendix 1.

All of the operations analysed were fully disbursed and allocated. A few required an extension period to allow the funds to be disbursed, but the extension was never significant and the operations were eventually allocated within acceptable time limits. The reasons for the extension varied and included; the need to improve internal IT systems and procedures to deal with GL requirements, over-estimated demand, and adequate training of the sales force. Most of these impediments were associated with new Bank counterparties and were not repeated in later operations.

Ex post vs ex ante dedication to COP objectives 2006-2008

| Operation no | 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
|---|---|---|---|---|---|---|---|---|---|---|
| Economic and Social Cohesion in the enlarged EU | • | • | ● | ● | ● | ● | ● | ● | ● | ● |
| Innovation 2010 Initiative (i2i) | ● | 47% | ● | | | • | • | • | • | • |
| Development of Trans-European and Access Networks | | | • | • | | ● | • | | • | • |
| SMEs or Micro | | | ● | ● | ● | | | ● | | ● |
| Environmental Sustainability | | 52% | • | | | • | • | • | • | |

□ ex-ante dedication (>70%)
● ex-post contribution to COP objecitves (>70%)
• ex-post contribution to COP objectives (between 20% and 70%)

Please note that:
(i) COP refers to Corporate Operational Plan 2006-2008 of the EIB.
(ii) For operation 2 the ex-ante dedication was min 70% i2i or Environment.

All FIs complied with the maximum ceiling for sub-loan project size. Similarly, all the operations were compliant with the Bank financing limit of up to a maximum of 50% of individual project cost. In one case (operation 10) the standard minimum project size of EUR 40,000 was waived to ensure that part of the loan reached micro-enterprises - the FI's core market segment.

The concentration of the allocated portfolios varied. Some FIs tended to target medium to larger borrowers within the SME market, as they represented a lower credit risk and were less costly to manage.

### 4.1.2. Terms and conditions

The operations varied significantly in terms of their basic characteristics.

**Structure -** The classic structure, consisting of a straight forward loan to an FI, was found in six operations (1,2, 3, 6, 7 and 9). In four cases (4, 5, 8 and 10) the Global Loan was instrumented utilising some form of a Loan Substitute. Loan Substitutes are an alternative means of providing funds to a project promoter or intermediary where the Bank subscribes to a Note issued by the Financial Intermediary itself or by a Special Purpose Vehicle (SPV), which in turn channels the funds and the financial advantage provided by the EIB to the Final Beneficiary. The Note is secured in various ways on a pool of underlying assets.

Three operations (4, 8 and 10) were structured via the purchase of a covered bond based on an underlying pool of mortgages. The value of this pool generally exceeds the value of the Bank's loan and this degree of over-collateralisation varied from one country to another according to the creditworthiness of the underlying assets (e.g. lower level of over-collateralisation was admitted where there was additional backing from public authorities' guarantees) and minimum requirements indicated by national law. However, all these products were of the highest credit quality and were accompanied by other forms of credit enhancements.

**Repayment mechanism -** In general, the Bank offered FIs the option between bullet and amortising loans and FIs showed a preference for bullet GLs, with only two operations selecting the amortizing alternative (operations 6 and 7).

**Interest rate -** All operations had a variable rate with fixed margin, except one with a fixed rate coupon (operation 6). In two cases (operations 6 and 7), the FI had the option to select the coupon rate (fixed rate, variable rate + variable margin, or variable rate + fixed margin) after contract signature. In one instance (operation 10), the contract foresaw a retrocession agreement between the Bank and the FI. In such case, the financial value added mainly consisted of the difference between the rate of the notes issued by the FI and purchased by the Bank and the EIB standard rate.

**Currency -** The availability of a range of currencies led some FIs to take advantage of short run pricing differentials. In some cases the Bank was able to provide more favourable terms by lending in USD rather than EUR.

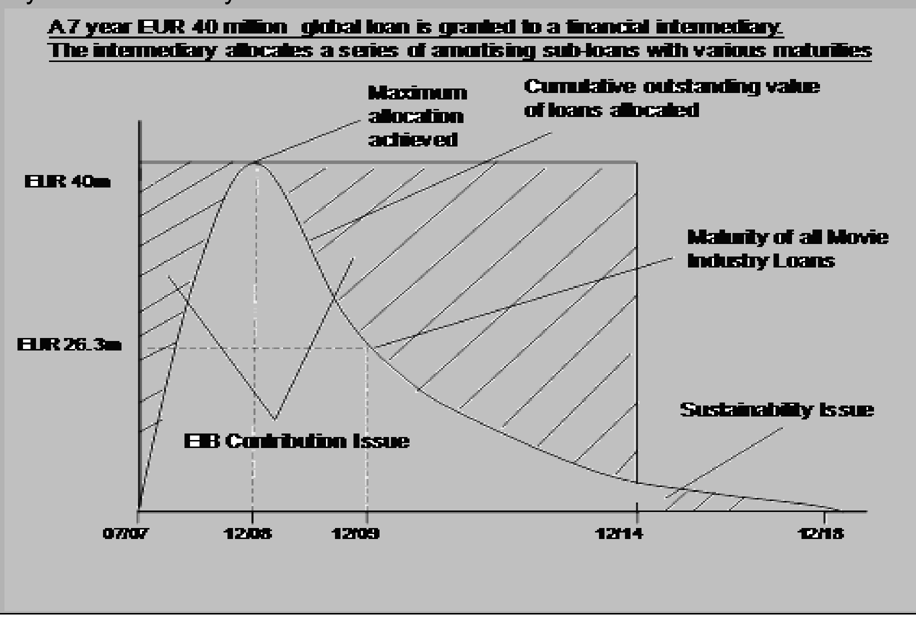
**Loan Term -** All the operations had a contractual maturity above seven years, which was considerably longer than the average maturity of the FI portfolios. Although it is impractical for the FIs to operate on a "back-to-back" basis, the availability of long term funding allows the FIs to further expand the loans to the SMEs segment as well as to exploit an interesting market niche. However, the impact that the longer duration of the Bank's loan had in increasing the volume of lending of the FIs however could not be quantified. Indeed, the Bank did not at that time routinely collect data on the maturity profile of the allocated portfolio.

**Case Study (operation 3) – Maturity mismatches (Germany's movie industry financing)**

The on lending conditions applied by the Financial Intermediary differed according to the type of project being financed as follows:

- "*Ganztagsschulprogramm*": The final beneficiary benefits from an interest free loan
- Modernisation of residential housing: The final beneficiary benefits from an interest free loan for the first 10 years
- Movie industry: Interest rate is based on the risk involved.

The tenor of the movie industry loans was short term, typically no more than a year. However loans for the other two categories tended to be in excess of 10 years. Where sub-loans for short periods (less than four year tenors) are granted, as illustrated in the diagram below, there is a financial benefit represented by the difference between the cost of funds of EIB and the financial intermediary applied to the unutilised funds of the dedicated Global Loan which is retained by the intermediary.



**Guarantee requirements -** For the sample analysed, guarantee arrangements were variable but all were compliant with the Bank's credit risk policy guidelines. Simple loans were either secured via assignments of rights or a pledge of acceptable securities. One operation (operation 3) was accepted as unsecured, the FI's obligations being covered by a statutory guarantee.

Loan Substitutes were accompanied by various credit enhancements and other contractual clauses. The seniority of the tranches purchased by the Bank always ranked "pari passu" with other co-senior investors. In addition, in all the cases evaluated, these structures foresaw an exit strategy via a put option in favour of the Bank.

Three operations required the assignment of rights. In one case this assignment related to the sub-projects financed via the Global Loan. For the others, the assignment was a so-called assignment of rights "décrochés", meaning that the original claims were independent of the allocation. This normally requires individual loans to be identified by the credit risk department in order to enable the Bank to monitor closely the quality and the validity of such assignments over the life of the loan.

### 4.1.3. On lending conditions

The Bank did not as a matter of course collect information on the terms of the on-lending (notably rate and maturity) regardless of the allocation procedure used. It follows that full data on pricing and maturities were not available and hence the analysis could not be extensive.

**Pricing -** In all cases there was sufficient anecdotal evidence that the funding advantage was passed on to the FBs. The mechanism adopted varied from one intermediary to another. There were only two cases in which the intermediary could demonstrate existing transparent procedures (operations 1 and 9) were in place to ensure that the treasury department identified, crystallised and credited the financial value added to a special account of the lending department. The financial value added was then dedicated to the reduction of interest rate on eligible loans allocated under the Global Loan only.

In one case (operation 8), the favourable on-lending conditions were assured by means of the FI participating in a promotional scheme provided by the national government requiring pre-defined maturity and maximum spreads for credit lines to SMEs.

In case of public sector financing, the FIs had to participate in public tender procedures, which are characterised by a high degree of price competition and level of transparency of pricing terms. The financial value added was then passed on via a reduction of interest rate on eligible loans allocated under the Global Loan or via other forms of financial advantage (e.g. no early repayment penalties). In one of the case visited (operation 6), the loan contract showed the rate applied was substantially lower than that of competitors, thus clearly demonstrating that there was a funding advantage being passed on to the FB.

**Loan term -** The EIB did not generally ask for information either on the maturity of the underlying capital investments or on the sub-loan financing the project. The implication is that a mismatch may occur between Global loans term and that of the projects financed. This provides a financial value added to the FI which is part of the overall attractiveness of the product. However, for the operations evaluated the extent of this advantage was not generally known and the Bank should investigate how this advantage could be passed on to the Final Beneficiaries.

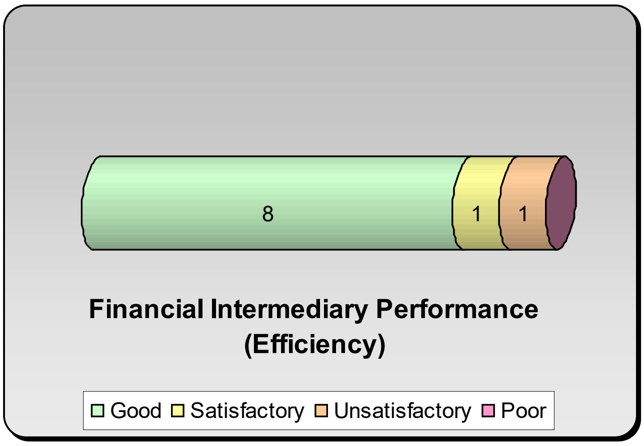
Such differences in duration should be reduced in the future. The interim solution, as already suggested in previous evaluation reports, is that the Bank requires, following full disbursement of the loan, a statement from the FI that it is continuing to develop its term lending in the sector(s) targeted by the GL, thus providing a proxy assurance that funds rolled over will continue to support the objectives of the GL.

### 4.1.4. Reporting

Reporting to EIB follows the applicable standard procedures which in general are well understood and complied with by the FIs. The majority of the information on FBs is supplied in the form of a list of allocations or individual operation fiches. The Portfolio approach was adopted only for one operation (operation 7). Under this approach FIs report globally on the development, volume and structure of their overall portfolio. The absence of detailed information relating to each allocation makes it difficult to quantitatively evaluate the outcomes of the operation. This type of reporting is now no longer used.

The Bank did not in general require FIs to send regular reports on sub-projects financed or information on the ex-post results of sub-projects when completed and FIs largely complied with the reporting requirements asked of them. The breakdown analysis of the allocation contains information that is largely based on the ex-ante information contained in the allocation list at the time of approval. The subsequent management of Final Beneficiaries was therefore largely delegated to the Financial Intermediary.

## 4.2. Financial Intermediary Performance (efficiency)




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

All operations except one were given ratings of Satisfactory or better for the Efficiency criterion. Eight operations were rated Good. Most of these were repeat operations and the FIs have shown on many occasions during last years their capability to implement EIB's objectives successfully. One operation (operation 1) was considered to be below expectations, largely due to financial distress faced by the Financial Intermediary at the time of the appraisal. However, it had subsequently significantly recovered.

### 4.2.1. Organisation and management

**Case Study (Operation 7) – Financing of small sized public facilities in regional development areas in France.**

For this operation, there were limited specific resources engaged and all reporting and follow up could be managed by a few individuals with a total estimated workload of a few man/weeks. This support was from the "Direction Commerciale" for customer details and from the "Direction d'Etudes" for macro reporting on loan operations and statistics. Each "Direction" spends approx 1 man week for preparing the reporting.

These costs are not specifically recharged to the final beneficiaries.

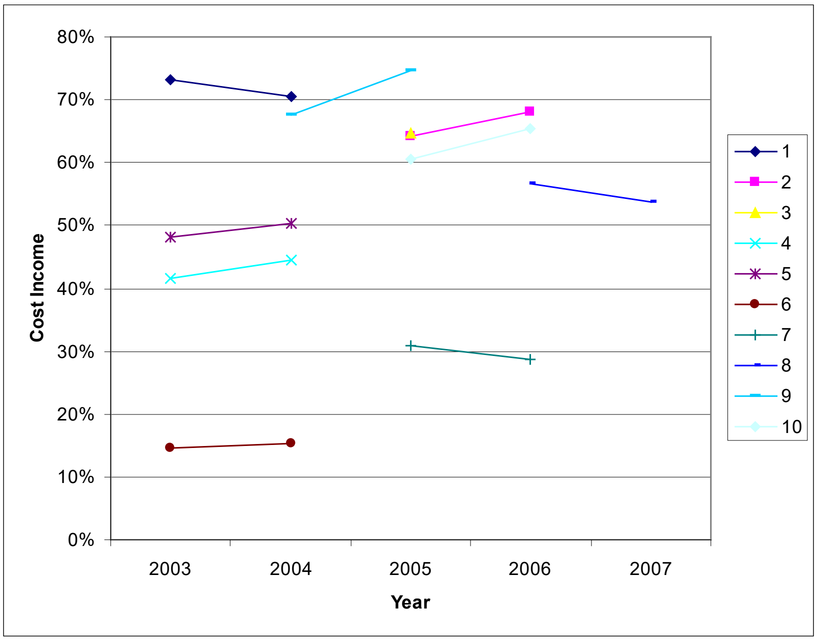
The management of the lines of credit by the FIs was satisfactory even for the new Bank's counterparties which were not familiar with GL criteria and quality standards. None of them required technical assistance to manage this type of facility. The quality of the management of the FIs is partly attributable to an effective process of identification and selection of the FI handled by the Bank. These processes were relatively straightforward in most of the operations due to the well established relationship with the FIs which derived from either previous GL operations or from successful business relationship with the FIs in direct lending.

The FIs selected are amongst the key players in their country in either public sector financing or SME financing, thus allowing a straightforward identification of sub-projects to be financed. For this reason, there was no evidence of a sub-optimal utilisation of the GLs.

In general, the allocations reflected the FIs' core business segment. There was only one exception to this general observation where the FIs did not have recognised experience in the field of the projects financed (operation 3).

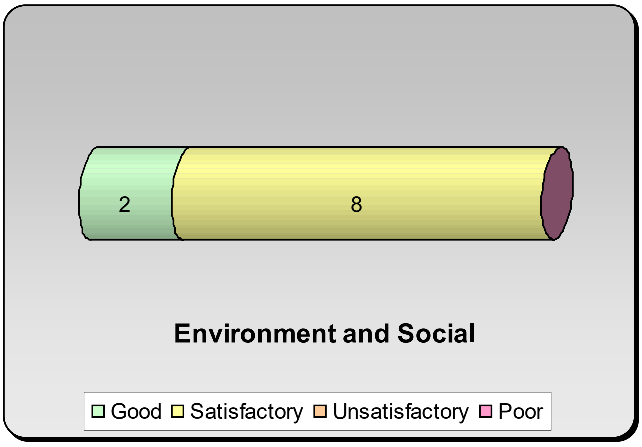
### 4.2.2. Financial situation

The evaluation focused on the **financial situation of the FIs at the time of the appraisal** or at signature through the use of widely accepted financial ratios to compare profitability, operating performance and key balance sheet and income statement data. Return on equity and cost income ratios (see figure below) varied significantly from one country to another, reflecting different levels of competition in the country or in the specific industry.




The majority of the FIs were rated A-equivalent or higher by rating agencies and all complied with normal prudential ratios - well above the regulatory minimum. The FIs evaluated were financially sound in all cases except one which had suffered operating losses and financial difficulties (operation 1). There was however no linkage between this situation and the financing that had been provided by the EIB. Such financial distress was transitory and the FI was already on the road to recovery at the time of the appraisal.

## 4.3. Environmental and Social Performance




*For Intermediated operations EIB delegates the verification of environmental and social compliance to its Financial Intermediaries, and the Environmental and Social criterion assesses the extent to which EIB requirements are understood by the Financial Intermediary and applied through its management procedures to sub loans.*

The awareness by FIs of EIB's standards and their enforcement, through written confirmation by the Final Beneficiary of compliance therewith, was rated Satisfactory or better in all cases. Indeed in two cases (operations 4 and 5) the FI demonstrated its capacity not only to manage operations in compliance with EU and/or national regulations but also to develop a proactive environmental approach and were therefore rated Good.

All operations examined were in compliance with EU and/or national guidelines, and many promoters had in place internal procedures and policies in relation to the environment, thus demonstrating an attention to environmental aspects and the commitment to avoid unnecessary pollution.

**Case Study (Operation 4) – Environmental procedures**

In 2001, the Financial Intermediary was one of the first institutions in the financial sector to incorporate an Environmental Management System, in accordance with the ISO 14001 standard, for all activities carried out in its main offices - as certified by AENOR in the same year. In 2007 the institution renewed this certification for another 3 years.

Its environmental policy has three basic priority lines of action:

- To minimize the waste generated and recycle all possible waste;
- To reduce the consumption of natural resources;
- To raise awareness and motivation among members, through training and awareness campaigns, to get them actively involved in responsible practices.

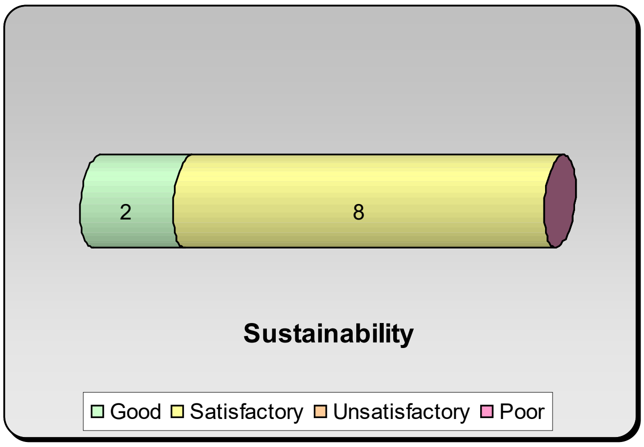
For the purposes of its credit risk internal scoring models, the Financial Intermediary also produces a sub-rating concerning the quality of the counterparty's environmental procedures.

The Bank requires that all projects that it finances comply at least with:

- Applicable national environmental law;
- Applicable EU environmental law,
- The principles and standards of relevant international environmental conventions incorporated into EU law.

All FIs were found to adhere to appropriate national guidelines which are integrated in their appraisal processes. Additionally the evaluation found two cases (operations 4 and 5) were the FI had established an internal environmental policy which applies to all its activities and an Environmental Management System fulfilling the requirements of ISO 14001: 2004. No sub-projects visited were found to have problems relating to environmental impacts.

## 4.4. Sustainability




*For intermediated operations the sustainability criterion looks at the likelihood that the Financial Intermediary will continue to operate successfully, that resources will be sufficient to maintain the outcome achieved over the economic life-time of the sub projects, and that any risks can be managed.*

All ten operations received a Satisfactory or better rating. In fact, despite the current economic crisis all of the FIs analysed remain financially sound.

The Good ratings reflect the particular FI's suitability as GL partner on a regional and country basis (operations 6 and 7) in which the FIs demonstrated their capacity to proactively identify operations by their leading and dynamic position, positively contributing to regional development.

### 4.4.1. Expectations (Pipeline)

In all cases, the relationship with the Bank fostered the already strong commitment of the FI on the targeted sectors. The evaluation did not find evidence that any of the FIs had started unwise expansion and/or diversification of its lending activities during the period following appraisal of the GL which would put at risk the continuity in the FIs activities or their sustainability as a GL partner.

### 4.4.2. Financial sustainability

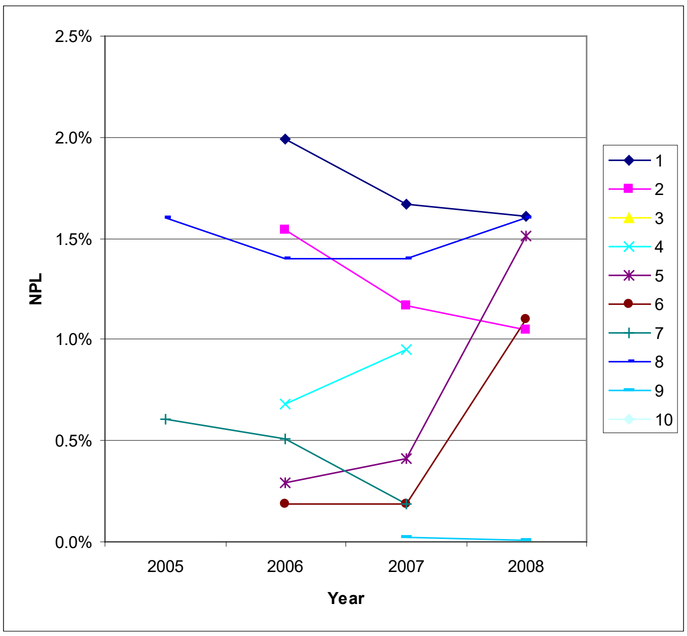
The individual analysis of FIs relied on observing the evolution of a broad spectrum of financial ratios. The evaluation focused on the FIs domestic franchise, its profitability and asset quality, its funding base and liquidity constraints, and the soundness of its capital base.

All the FIs evaluated were sustainable, supported by a good standing with the Bank and the various rating agencies. The low perceived level of banking sector risk in the countries in which the Global Loans were implemented, together with the essential contribution of the FIs to the banking sector, either at national- or regional-level, indicated a sustainable business in all cases.

### 4.4.3. Non Performing Loans

The level of non-performing loans was uneven throughout the sample (see figure below), but all FIs had satisfactory levels of credit losses, consistently below the average of the country or sector peers. Moreover, there was no evidence that the credit quality of the sub-loans granted was significantly different to the total loan portfolio of the FI. The gradual deterioration of the level of non performing loans experienced in the last year is strongly dependent on exogenous factors and does not impact the quality of the FIs to properly manage credit risk.

During the discussions with the FIs, additional information was collected on problem loans in the EIB financed portfolios, but it did not appear that this had been communicated to the Bank. This type of information should be regularly provided by the FI to the Bank by means of appropriate reporting.



### 4.4.4. Final Beneficiaries

The evaluation included a review of the FIs and a field visit to five Final Beneficiaries - one FB from each of five operations was selected and visited.

**Findings from Final Beneficiaries visits**

The five FBs visited were either Public Authorities or SMEs located in different countries and of different size.

In general, it is noted that:

- All FBs were satisfied with the service they had received;
- Most of the FBs had previous relationships with the FIs outside the EIB funding;
- All the FBs regarded the EIB contribution as beneficial in that favourable terms were achieved as regards tenor and rate;
- The availability of the term lending was instrumental in the financing of the eligible project visited;
- The FB compliance with the EIB's environmental and procurement requirements was primarily because the same requirements are enshrined in national legislation;
- In few cases the FIs had used the availability of EIB funding as a marketing tool;
- The involvement of EIB sometimes resulted in some incremental administration burden as compared to other borrowings of the FB. This was nevertheless deemed acceptable.

All the SMEs visited were operating in competitive markets, and many had positioned themselves well in their respective market segments by taking advantage of positive economic cycle during the past years. The investments had been well implemented and the FBs were achieving their operational objectives as well as servicing the loans. As regards regional development, the projects had contributed to direct and indirect employment but the latter was difficult to quantify without ex-ante development indicators.

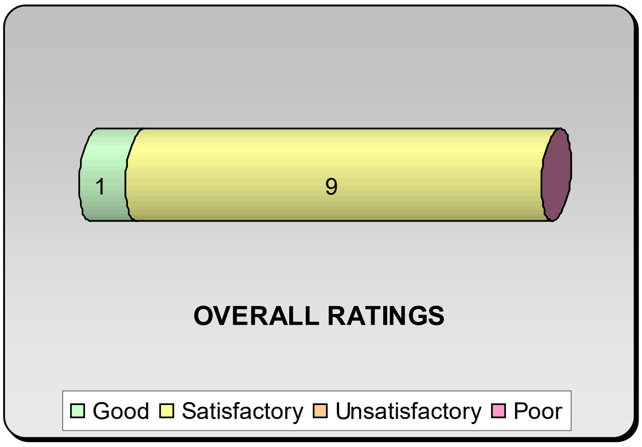
For the FBs the GLs value added was through increased access to longer-term finance in the form of loans or via price difference between taking the FI financing and financing from another bank. There were issues relating to the traceability of EIB funds in that at least in two cases (operations 6 and 8), the FBs were not aware of the EIB involvement. The absence of the notification however did not preclude site visits taking place during the evaluation.

**Case Study (Operation 5) – Financing for sundry equipment purchase** (Oil transportation sector)

The operation was channelled to SMEs in order to assist them with sundry equipment purchase for the development of their businesses.
The particular company visited was an SME active in the oil sector. Its business consists of oil distribution in the Galicia region, predominantly in the Coruña Province, for one of the foremost private oil companies in the world. The loan granted by the Financial Intermediary in the form of equipment leasing, was used to acquire four new oil tankers in order to comply with the oil company's tight environmental obligations. In line with the most recent international and European legislations on transport, the oil company requires its sub-contractors to have modern equipment and to regularly replace lorries and oil tankers (maximum life of 7 and 10 years respectively). This is aimed at reducing environmental impact (i.e. air, noise, and water pollution).
The Final Beneficiary, when interviewed, expressed its satisfaction for the financial conditions which were provided by the Financial Intermediary thanks for the EIB's involvement.

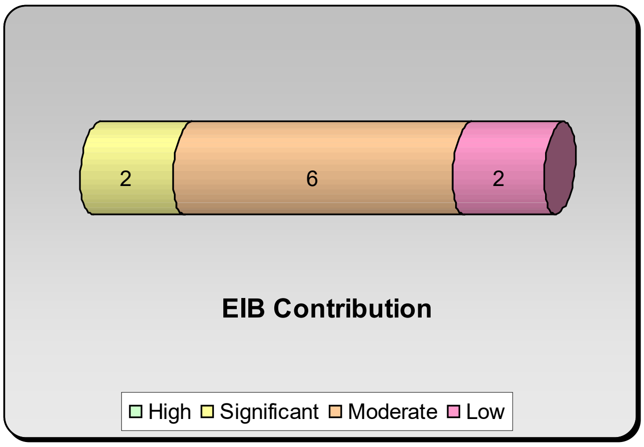
## 5. Overall Performance Ratings

***Ratings on relevance and operation performance:*** *As outlined in the introduction, the operations were evaluated on the basis of internationally accepted evaluation criteria of Relevance, Effectiveness, Efficiency and Sustainability. These individual ratings are considered together to produce an overall rating for the operation. 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 and Social aspects are rated separately, but are already accounted for within the four main ratings.*




All ten of the operations examined were fully disbursed and allocated and were rated as Satisfactory (or better in one case). In particular there was clear evidence that the EIB core objectives targeted through the Dedication of the operation had been achieved and in some cases exceeded. The Bank had shown considerable flexibility in its requirements to suit individual operations and Financial Intermediaries. Relationships were uniformly good, with repeat business being an important aspect of this type of operation. In most cases the Bank's added value was not significant, but there was no evidence of a lack of demand for the Dedicated Global Loan product. One operation (Operation 4) has been rated Good overall since the FI, despite being a new counterparty, demonstrated its ability to deal with the Bank's priorities and could rely on a sound and stable organisational and financial situation.

## 6. EIB Contribution




*The contribution which the EIB makes to the achievement of economically productive operations is both financial and non financial. This contribution is assumed to be positive and the criterion is therefore rated on a* ***four point positive scale*** *(high, significant, moderate and low). Both the financial and non financial component are considered equally important when arriving at an overall rating for the project or operation. Since the non financial contribution of the EIB to these types of operation is usually absent, this tends to bring down the overall rating – although it always remains positive.*

The Special Dedicate Global Loans facilitated the FIs' continued presence in the very competitive public sector and SMEs loan markets and enabled the FBs to achieve lower funding costs and longer tenors than otherwise. However, transparent processes were seldom in place to quantitatively determine the degree to which the EIB financial advantages are being passed onto the FBs and the evaluation therefore relied on indirect evidence. Also, for this type of operation, the institutional and technical contribution of the EIB is not significant in most cases. Two operations were therefore rated “Low”. Where the process of passing through EIB financial advantage was more transparent, or where a degree of non-financial support had been rendered, a rating of “Moderate” was assigned. Where there was a clearer indications of both a financial benefit to FBs together with some other EIB contribution, (operations 5 and 10), a rating of “Significant” was given.

## 6.1. Financial value added

### 6.1.1. Financial intermediary

The EIB financial value added usually takes three forms: currency, funding and term advantage.

**Currency** - The option to borrow in USD was taken by FIs pursuing short time pricing differentials.

**Funding** - There is not a widely accepted methodology to calculate the funding advantage and figures cannot be easily obtained as FIs were reluctant or unable to provide detailed figures. Previous evaluation reports have indicated a certain range of EIB funding advantage, and this evaluation confirms these estimates in broad terms for then operations examined. This advantage must be offset against the additional costs of working with the EIB. Apart from guarantee requirements, these include:

- Developing procedures for identifying suitable clients;
- Preparing new contracts for FBs, in line with the EIB's contract conditions;
- Managing the relationship with the EIB (including ex post valuation);
- Developing procedures for the operational units to comply with the Bank's eligibility requirements;
- Providing Allocation list information.

**Case Study (Project 8) – SME financing** (Portugal)

The participation in a promotional scheme provided by the Portuguese Government under PME Invest required the Financial Intermediary to offer particularly advantageous conditions in the loans offered to the final beneficiaries. Funding by the Bank was an important pre-requisite for the intermediary's participation in the national programme in view of the maturity and maximum spreads defined for such credit lines. Without the EIB funding, the maturity and spread that the commercial banks accepted to participate in the promotional scheme would have been different in view of the prevailing adverse market financial conditions. In addition, the very high implementation rate that has been achieved by the promotional scheme would have been different.

In other words, the financial advantage inherent in Bank funding enabled (and continues to enable) the Financial Intermediary to accommodate and accept the maturity and the maximum spreads required by the promotional scheme offered by the Portuguese Government. This was certainly the case also for the other major commercial banks that joined the promotional scheme - since the EIB has been keen to ensure a level playing field in the provision of its funding to the six leading commercial banks in Portugal.

It is likely that once these costs are included, the net funding advantage of the Bank becomes negligible, particularly for highly rated banks, and more likely to be influenced by other factors, such as the client effects, the competition in the industry, and the degree of risk associated with sub-projects.

Whilst the Bank could improve its funding advantage for this type of operation, for example by differential pricing based on the lower internal cost of this type of operation, or by reducing the quality of collateral required in appropriate cases. However, there is no evidence at the moment of a lack of demand for EIB funds, and there would be a concern that in providing even more attractive terms the Bank might be in danger of distorting the market.

**Loan Term** - The long maturity of the GL provides a substantial advantage where such long tenors are available to only a limited extent or not at all in the local financial markets. All operations examined were found to benefit from this advantage to a greater or lesser extent.

In conclusion, all the FIs acknowledged the presence of a financial value added from the EIB funding but they were rarely able to quantify it precisely. Additionally, the “funding value” was considered to be largely offset by the cost of complying with the Bank's loan requirements and credit risk guidelines.

### 6.1.2. Final Beneficiary

EIB did not as a matter of course seek data on the maturities and rates of the sub-loans allocated by the Financial Intermediary and therefore cannot quantitatively determine the degree to which the EIB financial advantages are being passed onto the Final Beneficiaries.

Notwithstanding, all of the operations provided sufficient anecdotal evidence of the Bank's funding advantage being passed on to the Final Beneficiaries. However, the evaluation also found that competition played a much more important role in providing lower costs to FBs than the funding advantage offered by the EIB. Only two had a transparent process for passing on the EIB funding advantage and one benefited from the EIB’s funding to enter into a national incentive scheme which required favourable conditions to be included into credit lines to SMEs.

**Case Study (Project 6) – Public Infrastructure maintenance works** (central Italy)

The evaluation of this operation included a field visit to a selected Final Beneficiary. The FB is a public authority located in central Italy to whom the Financial Intermediary provided two credit facilities.

The availability of such lending was instrumental in the financing of various maintenance works, both ordinary and extraordinary, in public infrastructures, as well as in public buildings (e.g. schools renovation project). The Final Beneficiary was able to provide all the relevant contractual and financial documentation in relation to the two facilities and to the final destination of the funds.

Both credit facilities were obtained following public tender procedures. The FB had recognised the favourable conditions provided by the Financial Intermediary in terms of a lower loan interest rate compared to other competitors. In particular for the smallest of the two credit facilities, the Financial Intermediary provided a significant value added due to the fact that the bank did not requested penalties in case of early repayment.

However, the FB was not informed of the EIB contribution and that such information was not disclosed in the contract. The FB hence became aware of EIB’s involvement just before the evaluation field visit.

The notification of EIB involvement is a standard Bank requirement following the transparency objective set out in 2000, and this obligation is systematically included in the finance contract or side letter, which in turn gives the right of visit to the FI. However, ex post the FB’s were not always informed or aware of the use of EIB funding for their loans. In any case, advising FBs at the contract negotiation stage that the funding will partly come from the EIB is too late to influence their decisions.

There were significant obstacles to tracing the Bank’s added value through to Final Beneficiaries, such as the lack of information on the outcome of sub-projects, the arms length relationship between the Bank and FBs, and the previously mentioned issues relating to allocations for credit lines where certain key information is not routinely collected.

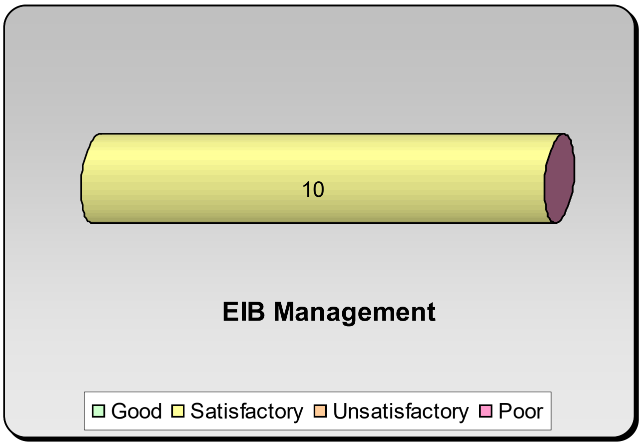
During field visits it was mentioned that the Bank might envisage moving towards more flexible forms of intervention in the SME segment (e.g. short term back-up facility and/or risk sharing) to deal with current market conditions and offer greater value added to the FB. This could only be done by working closely with FIs in areas such as product development.

### 6.2. Institutional and Technical Contribution

This contribution relates to any significant non-financial contribution to the operation provided by the EIB. It may take the form of improvements of the technical, economic or other aspects of the operation.

Non-financial value added was evidenced in the operation 10 where the Bank was able to transfer know-how and facilitate the set up of the facility through its expertise as well as its privileged contact to National Authorities. In the other operations, the non financial value added was less significant, although the close collaboration between the Bank's operational staff with the new FIs allowed these latter to efficiently handle the funding and to comply with the GL's requirements.

## 7. EIB Operation Cycle Management




*This criterion assesses the way in which EIB identifies, appraises and monitors its operations. The current EIB operation cycle management approach has been developed over a long period of time and is being continuously developed and improved to meet new challenges. The approach is systematic, structured and well adapted to the vast majority of the Bank's operations. In all operations evaluated the Bank's management of the process was considered as broadly Satisfactory, with occasionally minor problems being offset by additional efforts in other areas.*

The Bank had good and long established relationships with most of the Financial Intermediaries and the appraisal was well structured. Although the overall Bank's performance on operation-cycle management is considered Satisfactory for the operations evaluated, certain weaknesses in the management of the operation cycle were noticeable, particularly in the quality of monitoring and reporting activities.

### 7.1. Operation Identification

In all the cases, the operation identification was a straightforward process. The Bank relied on its knowledge of suitably experienced FIs in the domestic financial markets to identify and implement the operation. The operations were generally one element of the Bank's business relationship with the FIs, which often also included loan intermediation or guarantees for direct operations.

Notwithstanding, the depth of understanding of the FIs' business, operations and strategies was not evenly distributed amongst operational staff and was more often associated with longstanding members of staff rather than with the Bank's systems and documentation. This might have some impact on the quality and the availability of project related information and the Bank should review its handover procedures and client data to reduce this reliance on individual knowledge.

### 7.2. Selection of Financial Intermediary

Eight of the GLs in the sample were repeat operations and therefore selection of the FIs was largely based on the past performance. The selection of the new FIs (operations 4 and 5) was linked to the successful business relationship established in other operations and it was made in the context of Board of Director's recommendations to foster diversification of its counterparts in Global loans operations dedicated to SMEs. At the same time, it followed the FIs desired to become an active and regular partner with the Bank.

The Evaluation found that ongoing management and organisational issues were sufficiently addressed during the Bank's appraisal. While sometimes lacking depth in the analysis with regard to sector and market analysis (i.e. demand side and handling of the FI), the Board Reports and Financial Notes provided sufficient information on FIs organisation, management, processes and risk management governance.

### 7.3. Operation Approval Process

The appraisals carried out by the Bank were satisfactory. Indeed all operations showed the capacity of the Bank to complete the approval process quickly and smoothly. The potential issues requiring special attention were clearly identified in the appraisal process. This is also true for the two operations which experienced complications that are often involved in the setting up of a GL. One of them related to the need to extend the "caducité" date for operation 5. This was linked to exogenous factors and involved a new counterparty. The other (operation 10) was associated with the complex set up of the financial structures which required additional investigation and extensive due diligence. It has to be noted that detailed information on specific sectors targeted by the operation would have enabled a sounder grasp on the ability of the FIs of handling EIB funds.

No significant differences were found between the credit analysis carried out by the Bank for repeat operations and for new counterparties, but for the former, equivalent information was less evident. The Board Report considered the financial situation of the FI and any significant change occurring since the last appraisal. In addition, for repeat operations a summary of the use of the previous Global Loan was included.

### 7.4. Monitoring and reporting

The Bank's approach to the post signature management of its Global Loan operations is designed to minimise the administrative burden on both the FI and on Bank staff, whilst at the same time gathering sufficient information to ensure compliance with its requirements. This involves a period of intense activity during the time that the loan is being allocated, but thereafter the Bank relies entirely on the Financial Intermediary to notify it of any relevant changes. More recently, this has been supplemented by a more pro active approach on the monitoring of the quality of collateral in certain cases.

The Bank's finance contract usually required the FI to provide its report and accounts annually, but compliance with this requirement was not assured and the financial situation of FIs was not always regularly reviewed (particularly in the case where there were no new operations with the same counterparty).

Although no fundamental problems were identified in the performance of the ten operations examined, the evaluation found a number of areas where improvements could beneficially be made to the monitoring and reporting process:

- The reporting requirements specified by the different operational units of the Bank were quite heterogeneous, although there were some common requirements;
- Certain key data such as sub loan maturity, interest rate or non performing loans were not systematically requested;
- The dossiers in the Bank's IT system were well structured and should have included all relevant documentation, but there were many gaps, particularly in the area of allocation reporting;

- Where the allocation list was provided electronically, this was not always stored in the archive dossier, and there was no record in the dossier of where the electronic data is being held.
- Key operational information often resided with experienced members of staff rather than in the Bank's systems;
- There was no quantitative evidence in the archived documents of the passing-on of part of the EIB funding advantage by the FI to the FB. Although this subject might have been raised by the operational staff and discussed in depth with all FIs it was not necessarily documented.
- Beyond the initial allocation the EIB does not require FIs to send any subsequent reports on sub-projects financed or information on the ex-post results of sub-projects when completed.
- Few FIs provided regular reports on their own financial situation and, although the EIB was entitled to request such information, this right was rarely exercised.
- For repeat operations, the Board Report for the subsequent operation almost always contains a short paragraph about the previous operation. The focus is on the allocation process, highlighting the number of allocations and the proportion of funding which had gone to eligible investments. Otherwise, the Bank's reporting of its GL operations in member States was confined to an annual summary of activities, which has been discontinued since 2006.

The Bank should review its documentation requirements for Global loans with a view to on the one hand streamlining the process, and on the other hand collecting additional key data. It is recognised that many of these issues have already been addressed in the new Global Loan for SMEs product, although it is too soon to draw any conclusions on the practical implications of the new product for systematic documentation. However, it is clear that changes will have to be carried through at the level of detailed operating procedures in order to have the required impact, and should incorporate the following elements:

- Information requirements should be standardised and should include data on maturity, interest rates, currency, prepayments and non-performing loans.
- The process of transferring allocation information should as far as possible be automated to avoid manual transcription.
- The practice of reporting on the ex ante allocation of previous GLs during the approval of subsequent operations should be replaced with a regular and standardised reporting procedure for all GL operations containing current allocation information.
- Better use should be made of the Bank's existing electronic tools to record systematically, on a cross directorate basis, key post signature operational activity. This will facilitate dissemination of operational information and assist in the handover of operations to new staff.
- The annual management report on global loans should be reinstated, based on improved data capture to facilitate the process.
- The Bank should examine a reasonable sample of Final Beneficiaries ex post.

### 7.5. Note on ongoing relationship with the Financial Intermediary

The evaluation did not highlight any significant issues with respect to the Financial Intermediaries. The relationship with EIB had so far been deemed successful and in most of the cases, the operations evaluated were followed by other Global Loans with the Bank.

Personal contacts between the Banks and FIs seem to be well established. From the meetings with the various FIs, we can conclude that they all value the relationship with the EIB and they are attentive to the requirements of the GL product. Management was accessible and prone to provide insightful suggestions on how to strengthen the relationship with the Bank. The requested information was mostly available during the meeting or shortly thereafter.

## Appendix 1: Ex Post Dedications

| Op. No | Ex Ante | Ex Post | Comments |
|---|---|---|---|
| 1 | • small and medium sized projects promoted by the public sector<br>• Target to innovation 2010 initiative, education and training, research and development. | • small and medium sized projects promoted by the public sector such local authorities<br>• Projects were targeted mainly at the education sector (schools as well as universities), where infrastructure enhancement was increasingly a priority in Germany. | • Achieved<br>• Financing of school renovations is deemed to improve “access to quality education and training”, one of the three objectives of the i2i initiative. Therefore the indicated dedication was achieved. |
| 2 | • Target to small-scale eligible investments in the fields of:<br>at least 70% innovation 2010 initiative (“i2i”) or Environment,<br>less that 30% health.<br>• Regional development in Hesse and Thuringia also other areas in Germany and in other EU Member States were also eligible.<br>• Dedicated tranches for projects implemented via PPP structures. | • small and medium sized projects promoted by the public sector such local authorities<br>• 52% allocation to environmental loans<br>47% allocation to school building/renovations<br>• No funding of PPP structures was achieved. | • Achieved<br>• Here again, school renovation is deemed to improve “access to quality education and training”. It is noted that financing provided to meet the other two objectives (see bullet points below in Figure 6) that define i2i is lacking when the loan allocations are analysed. |
| 3 | • Co-financing (up to 50% of external financing) of small and medium-sized enterprises (SMEs), alongside the commercial banks<br>• Targeted domain: social housing and urban renewal, health, and education.<br>• Small-scale projects in the fields of Innovation 2010 Initiative (“i2i”), environmental protection, energy and infrastructure in Brandenburg.<br>• Regional development (State of Brandenburg - convergence region) | • Financing limited to 50% of project cost<br>• 31% "Ganztagsschulprogram"<br>35% modernisation of residential housing<br>34% movie industry<br>eligibility criteria and the specific requirements of the global loan instrument are adhered to | • Achieved<br>• The allocation objective with respect to financing Economic & Social Cohesion / Regional development projects appears to have been met. |

| Op. No | Ex Ante | Ex Post | Comments |
|---|---|---|---|
| 4 | • Objective to finance projects of limited scale promoted by SMEs (70%) and local authorities<br>• Over 70% regional development zones in Spain defined as Objective 1 and 2 areas | • 87% SME<br>5% local authorities<br>• More than 70% allocations addressed in objectives 1 and objectives 2 areas, of which 50% on the transport and manufacturing sectors | • Achieved |
| 5 | • Finance projects of limited scale promoted by SMEs and local authorities throughout Spain<br>• 70% of the global loan to projects in Objective 1 and 2 areas of Spain | • All the projects financed were addressed to SMEs.<br>• Objective 1: 47%<br>Objective 2: 28% | • Large number of final beneficiaries (1005)<br>• Fully compliant. |
| 6 | • Small and medium sized infrastructure project of regional development or Community interest throughout Italy with a special focus on regional development (to which at least 70% of the facility is dedicated) | • 45% local or regional authorities<br>54% public operational companies<br>• Approx 25% dedicated to the regional development of the "Mezzogiorno" region (objective 1 region).<br>• More than 70% dedicated to infrastructures projects of regional development or community interest covering the following sectors: environment, energy, education, transport and health | |
| 7 | • Public authorities<br>• Small-sized public facilities in areas such as transit, environmental protection, social housing, health, education in regional development areas | • Achieved<br>• The loans were mainly used to finance projects in transit, utilities, environment, health and education sectors so that the indicated dedication is achieved. | • Reporting based on operation portfolio, so that the dedication, although highly probable given the corporate objectives and experience if the FI, cannot be fully substantiated. |
| 8 | • SMEs<br>• Regional development by supporting lending to SMEs for equipment purchase | • 75% SME<br>25% public local authorities<br>• Achieved.<br>• In various cases the funding was provided for projects directly connected with other | • Approx 3% of the allocations mobilized around 40% of all loans granted. |

| Op. No | Ex Ante | Ex Post | Comments |
|---|---|---|---|
| | | EIB priorities (i2i, energy savings, renewable energies and environment protection). | |
| 9 | • 20% SMEs<br>• Projects of limited scale in fields of infrastructure improvement, environmental protection and improvement, the rational use of energy, health and education.<br>• Regional development situated in Austria and other EU Member States (70%) | • Approx 75% of the allocations have been made within assisted areas. | • Evidence was not provided to confirm whether the initial target of 20% of allocations to SMEs has been satisfied. However, this was not the main dedication. |
| 10 | • SMEs and micro-enterprise market segment<br>• Regional development - all regions in Poland (Convergence objective in the country) | • 70% SMEs 30% Micro-enterprises<br>• The sectors covered by the allocations are the following: transport (68%), construction, health and others. | • leasing activities |

## Appendix 2: Evaluation Process and Criteria

In accordance with EV's Terms of Reference, the objectives of evaluation are:

- To assess the quality of the operations financed, which is assessed using generally accepted evaluation criteria, in particular those developed by the Evaluation Cooperation Group, which brings together the evaluation offices of the multilateral development banks. The criteria are:

  **a)** **Relevance** corresponding to the first pillar of value added*:* is the extent to which the objectives of a project are consistent with EU policies, as defined by the Treaty, Directives, Council Decisions, Mandates, etc., the decisions of the EIB Governors, as well as the beneficiaries' requirements, country needs, global priorities and partners' policies. In the EU, reference is made to the relevant EU and EIB policies and specifically to the EU Treaty that defines the mission of the Bank. Outside the Union, the main references are the policy objectives considered in the relevant mandates.

  **b)** Project performance, measured through **Effectiveness (efficacy)**, **Efficiency** and **Sustainability** and second pillar of value added*.*

  Effectiveness relates to 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.

  Efficiency concerns the extent to which project benefits/outputs are commensurate with resources/inputs. At ex-ante appraisal, project efficiency is normally measured through the economic and financial rates of return. In public sector projects a financial rate of return is often not calculated ex-ante, in which case the efficiency of the project is estimated by a cost effectiveness analysis.

  Sustainability is the likelihood of continued long-term benefits and the resilience to risk over the intended life of the project. The assessment of project sustainability varies substantially from case to case depending on circumstances, and takes into account the issues identified in the ex-ante due-diligence carried out by the Bank.

  Environmental and Social Impact of the projects evaluated and specifically considers two categories: (a) compliance with guidelines, including EU and/or national as well as Bank guidelines, and (b) environmental performance, including the relationship between ex ante expectations and ex post findings, and the extent to which residual impacts are broadly similar, worse or even better than anticipated.

  Evaluations take due account of the analytical criteria used in the ex-ante project appraisal and the strategy, policies and procedures that relate to the operations evaluated. Changes in EIB policies or procedures following project appraisal, which are relevant to the assessment of the project, will also be taken into account.

- to assess the EIB contribution *(Third Pillar)* and management of the project cycle:

  **EIB Financial contribution** *identifies the financial contribution provided in relation to the alternatives available, including improvements on financial aspects as facilitating co-financing from other sources (catalytic effect).*

  **Other EIB contribution (optional)** relates to any significant non-financial contribution to the operation provided by the EIB; it may take the form of improvements of the technical, economic or other aspects of the project.

  **EIB Management of the project cycle** rates the Bank's handling of the operation, from project identification and selection to post completion monitoring.

**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.
The following thematic ex-post evaluations are published on the EIB Website:

1. Performance of a Sample of Nine Sewage Treatment Plants in European Union Member Countries (1996 - available in English, French and German)
2. Evaluation of 10 Operations in the Telecommunications Sector in EU Member States (1998 - available in English, French and German)
3. Contribution of Large Rail and Road Infrastructure to Regional Development (1998 - available in English, French and German)
4. Evaluation of Industrial Projects Financed by the European Investment Bank under the Objective of Regional Development (1998 - available in English, French and German)
5. An Evaluation Study of 17 Water Projects located around the Mediterranean (1999 - available in English, French, German, Italian and Spanish).
6. The impact of EIB Borrowing Operations on the Integration of New Capital Markets. (1999 – available in English, French and German).
7. EIB Contribution to Regional Development A synthesis report on the regional development impact of EIB funding on 17 projects in Portugal and Italy (2001 – available in English (original version), French, German, Italian and Portuguese (translations from the original version)).
8. Evaluation of the risk capital operations carried out by the EIB in four ACP countries 1989-1999 (2001 - available in English (original version), French and German (translations from the original version)).
9. EIB financing of energy projects in the European Union and Central and Eastern Europe (2001- available in English (original version), French and German (translations from the original version))
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14. EIB Financing of Urban Development Projects in the EU (2003 – available in English (original version), French and German (translations from the original version)).
15. Evaluation of the Projects Financed by the EIB under the Asia and Latin America Mandates (2004 – available in English (original version), French, German and Spanish).
16. Evaluation of EIB Financing of Airlines (2004 – available in English (original version) French and German)
17. Evaluation of EIB Financing of Air Infrastructure (2005 - available in English (original version) German and French)
18. EIB financing with own resources through global loans under Mediterranean mandates (2005 - available in English (original version) German and French.)

19. Evaluation of EIB Financing of Railway Projects in the European Union (2005 - available in English (original version) German and French.)
20. Evaluation of PPP projects financed by the EIB (2005 - available in English (original version) German and French).
21. Evaluation of SME Global Loans in the Enlarged Union (2005 - available in English (original version) and German and French.)
22. EIB financing with own resources through individual loans under Mediterranean mandates (2005 - available in English (original version) and German and French.)
23. Evaluation of EIB financing through individual loans under the Lomé IV Convention (2006 - available in English (original version) German and French.)
24. Evaluation of EIB financing through global loans under the Lomé IV Convention (2006 - available in English (original version) German and French.)
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27. FEMIP Trust Fund (2006 - available in English.)
28. Evaluation of Borrowing and Lending in Rand (2007 - available in English (original version) German and French).
29. Evaluation of EIB Financing of Health Projects (2007 - available in English (original version) German and French).
30. Economic and Social Cohesion - EIB financing of operations in Objective 1 and Objective 2 areas in Germany, Ireland and Spain (2007 - available in English. (original version) German and French)
31. Evaluation of EIB i2i Research, Development and Innovation (RDI) projects (2007 - available in English)
32. FEMIP Trust Fund - Evaluation of Activities at 30.09.2007 (2007 - available in English.)
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